EDITOR'S NOTE

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o. 86-71-AFX
tatus: GRANTED

Title: CTS Corporation, Appellant
v.
Dynamics Corporation of America, et al.

ocketed:
uly 21, 1986

Court: United States Court of Appeals
for the Seventh Circuit

ide:
86-97

Counsel for appellant: Strain, James A., Pritchard, John F.

Counsel for appellee: Sachnoff, Lowell E.

ntry	Date	Note	Proceedings and Orders
1	Jul 21 1986	G	Statement as to jurisdiction filed.
2	Jul 21 1986		Appendix of appellant CTS Corp. filed.
3	Aug 25 1986		Motion of appellee Dynamics Corp. of Am. to affirm filed. VIDED.
4	Aug 25 1986		Appendix of appellee Dynamics Copr. of America filed. VIDED.
5	Sep 3 1986		DISTRIBUTED. September 29, 1986
6	Sep 3 1986		REDISTRIBUTED. September 29, 1986
7	Sep 2 1986		Lodging received.
8	Sep 5 1986	X	Reply brief of appellant CTS Corp. filed.
9	Oct 6 1986		PROBABLE JURISDICTION NOTED. The case is consolidated with 86-97, and a total of one hour is allotted for oral argument. Justice Scalia OUT. ***
11	Nov 6 1986		Order extending time to file brief of appellant on the merits until December 4, 1986.
12	Oct 17 1986	G	Motion of appellant to dispense with printing the joint appendix filed.
13	Nov 17 1986		Motion of appellant to dispense with printing the joint appendix GRANTED.
14	Nov 20 1986		Record filed.
15	Nov 20 1986		Certified copy of C. A. proceedings received.
16	Dec 4 1986		Brief of appellant CTS Corp. filed.
17	Dec 4 1986		Brief amicus curiae of New York filed. VIDED.
18	Dec 4 1986		Brief amicus curiae of Minnesota filed. VIDED.
19	Dec 3 1986		Brief amicus curiae of Indiana Chamber of Commerce, et al. filed. VIDED.
21	Dec 19 1986		Order extending time to file brief of appellee on the merits until January 20, 1987.
23	Dec 20 1986	G	Motion of appellants for divided argument filed.
24	Dec 19 1986		SET FOR ARGUMENT. Monday, March 2, 1987. This case is consolidated with No. 86-97. (3rd case) (1 hour).
25	Jan 15 1987		Record filed.
26	Jan 15 1987		Certified copy of original record on appeal received. (3 boxes).
27	Jan 20 1987		Brief amicus curiae of United Shareholders Assn. filed. VIDED.
28	Jan 20 1987		Brief amicus curiae of United States filed. VIDED.
29	Jan 22 1987		CIRCULATED.
30	Jan 20 1987	X	Brief amicus curiae of Securities Industry filed. VIDED.
31	Jan 20 1987	X	Brief of appellee Dynamics Corp. of America filed. VIDED.

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ntry	Date	Note	Proceedings and Orders
32	Feb 23 1987		Motion of appellants for divided argument GRANTED.
33	Feb 23 1987	X	Reply brief of appellant CTS Corp. filed.
34	Mar 2 1987		ARGUED.

86-71 (1)

No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

JURISDICTIONAL STATEMENT OF APPELLANT CTS CORPORATION

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QUESTIONS PRESENTED

1. Whether the Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE ANN. §§ 23-1-42-1 to -11 (Burns Cum. Supp. 1986), which makes the post-acquisition voting rights of "control shares" in covered Indiana corporations subject to a majority vote of all shareholders other than the acquiring entity and incumbent management, but does not regulate disclosures to shareholders or the purchase of shares, is unconstitutional under the Supremacy Clause because preempted by the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f), which regulates only disclosures to shareholders and the purchase of shares in tender offers.

2. Whether the Control Share Acquisitions Chapter, which does not discriminate against interstate commerce or out-of-State residents, applies only to Indiana corporations with other substantial ties to the State, and regulates shareholder voting rights as a matter of the State's generic corporation law governing the internal affairs of Indiana corporations, is unconstitutional under the Commerce Clause.

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OPINIONS BELOW

The United States Court of Appeals for the Seventh Circuit issued its final opinion on June 9, 1986. The opinion, which has not yet been published, is set forth in the separately-bound Appendix to Jurisdictional Statement of Appellant CTS Corporation ("Appendix") at A1. The two not-yet-published opinions of the United States District Court for the Northern District of Illinois on the questions presented were issued on April 9 and April 16, 1986, and are set forth in the Appendix at A29 and A88.

JURISDICTION

This is a civil action commenced in the United States District Court for the Northern District of Illinois by appellee Dynamics Corporation of America ("DCA") against appellant CTS Corporation ("CTS") and others.[1] DCA's complaint, as

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[1] *Rule 15.1(b) Listing:* In Seventh Circuit No. 86-1601, which involved the constitutional questions presented by this appeal to the Supreme Court, the parties in the Seventh Circuit were DCA, as plaintiff-appellee; CTS, Robert Hostetler, Gary Erekson, and Joseph DiGirolamo (officers and/or directors of CTS), as defendants-appellants; and the State of Indiana, as intervenor-appellant.

Seventh Circuit No. 86-1608 involved the same action in the District Court and was consolidated with No. 86-1601 for decision by the Seventh Circuit, but did not involve the constitutional questions presented by the present appeal. In No. 86-1608, the parties in the Seventh Circuit were DCA; Andrew Lozyniak, Edward J. Mooney, Henry V. Kensing, Patrick J. Dorme, Frank A. Gunter, Curtis T. Roff, Saul Sperber, Joseph P. Walker and Harold Cohan (officers and/or directors of DCA); CTS; and Robert D. Hostetler, Gary B. Erekson, Joseph DiGirolamo, George F. Sommer, Gerald H. Frieling, Jr., Don J. Kacek, Ted Ross and Richard M. Ringoen (officers and/or directors of CTS).

Rule 28.1 Listing. Appellant CTS Corporation has no parent corporation, non-wholly owned subsidiaries, or affiliates.

Rule 28.4(c) Statement: 28 U.S.C. § 2403(b) may be applicable to this appeal. The State of Indiana intervened as appellant in the

(Footnote continued on following page)

amended, alleged violations of the Federal securities laws, pendent State-law claims, and that the Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE ANN. §§ 23-1-42-1 to -11 (Burns Cum. Supp. 1986), violates the Supremacy and Commerce Clauses of the Constitution of the United States. Federal jurisdiction was based upon 15 U.S.C. § 78aa, 28 U.S.C. §§ 1331 & 1332, and the doctrine of pendent jurisdiction. The constitutional claim is the only claim pertinent to this appeal.

The judgment of the United States Court of Appeals for the Seventh Circuit ("Seventh Circuit"), entered April 23, 1986, held the State statute unconstitutional on both Supremacy and Commerce Clause grounds. Appendix at A126. On July 16, 1986, CTS filed in the Seventh Circuit its notice of appeal to this Court. Appendix at A133. The Supreme Court has jurisdiction of this appeal pursuant to 28 U.S.C. § 1254(2).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The following constitutional provisions and statutes are involved, the texts of which are set forth in the Appendix at A140:

1. The Commerce Clause, U.S. CONST. art. I, § 8, cl. 3.

2. The Supremacy Clause, U.S. CONST. art. VI, cl. 2

3. The Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f).

4. The Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE ANN. §§ 23-1-42-1 to -11 (Burns Cum. Supp. 1986).

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Seventh Circuit to defend the State statute. The State of Indiana then filed in the Seventh Circuit a separate Notice Of Appeal to this Court. Counsel for CTS is presently informed that the State will file a separate Jurisdictional Statement with this Court.

STATEMENT OF THE CASE

A. General Background.

Appellant CTS is an Indiana corporation with its principal place of business in Indiana. Appellee DCA is a New York corporation with its principal place of business in Connecticut. On March 10, 1986, DCA, then the beneficial owner of approximately 9.6% of the outstanding shares of CTS's single class of stock, announced a combination partial tender offer and proxy contest. DCA's tender offer sought one million shares of CTS stock, which would give it approximately 27.5% of the outstanding CTS shares. DCA's proxy contest sought to replace CTS's entire board of directors with a slate proposed by DCA at CTS's annual shareholders meeting then scheduled for April 25, 1986 (the "Annual Meeting").

On March 4, 1986, prior to DCA's announcement, the Governor of Indiana signed into law the new Indiana Business Corporation Law, IND. CODE ANN. §§ 23-1-17-1 to 23-1-54-2 (Burns Cum. Supp. 1986), a comprehensive revision of the State's generic corporation code. Mandatory application of the new law to Indiana corporations begins August 1, 1987, but corporations may elect to be governed by it before that date. *See* IND. CODE ANN. § 23-1-17-3. On March 27, 1986, CTS elected to be covered by the new law effective April 2, 1986. The courts below held unconstitutional the Control Share Acquisitions Chapter of the new law, IND. CODE ANN. §§ 23-1-42-1 to -11 ("Control Share Chapter").

B. The Control Share Chapter.

The Control Share Chapter governs the voting power of "control shares" of certain Indiana corporations. It does not restrict or otherwise regulate the purchase or sale of such shares, whether in a tender offer or otherwise. "Control shares" are any shares that, when added to the acquiring person's previous holdings, pass any one of three thresholds — 20%, 33.3%, or 50% — of voting strength in electing the corporation's

board of directors. IND. CODE ANN. § 23-1-42-1. The Control Share Chapter applies only to an "issuing public corporation," defined as an Indiana corporation that has:

(1) 100 or more shareholders;

(2) its principal office, principal place of business, or substantial assets in Indiana; *and*

(3) either more than 10% of its shares owned by Indiana residents, or more than 10% of its shareholders resident in Indiana, or more than 10,000 shareholders resident in Indiana.

See IND. CODE ANN. § 23-1-42-4(a).[2]

Substantively, the Control Share Chapter provides that "[c]ontrol shares have the same voting rights as were allocated the shares before the control share acquisition only to the extent granted by resolution approved by the shareholders of the issuing public corporation." IND. CODE ANN. § 23-1-42-9(a). Since the one million shares sought (and later purchased) by DCA pursuant to its tender offer put DCA over the 20% threshold, the voting power of those "control shares" must be determined by a shareholder vote that excludes "all interested shares" — *i.e.*, shares owned by officers of the corporation, directors who are also employees of the corporation, and the acquiring person. IND. CODE ANN. §§ 23-1-42-9(b)(2) (shareholder vote) & -42-3 (defining "interested shares"). Thus, under the Chapter, DCA may not vote its newly-acquired

[2] The term "corporation" as used in the Control Share Chapter is defined for purposes of the entire Business Corporation Law as "a corporation for profit that is not a foreign corporation." IND. CODE ANN. § 23-1-20-5. The District Court had erroneously concluded that the Control Share Chapter could be applied to foreign corporations. The Seventh Circuit corrected this error and held, as the plain language provides, that the Chapter applies only to Indiana corporations.

shares until it receives a majority vote of approval by the remaining CTS shareholders who are affiliated with neither CTS management nor DCA.[3]

The Control Share Chapter creates a mechanism for a prompt vote by the disinterested shareholders on the voting rights of the control shares. At any time before, during, or after its acquisition of control shares, the acquiring person may file an "acquiring person statement" with the company. IND. CODE ANN. § 23-1-42-6. Upon request of the acquiring person, a special shareholders meeting to decide the voting rights of the control shares must be held no later than fifty days after the company receives the statement. IND. CODE ANN. § 23-1-42-7. If no special meeting is requested, the issue will be decided at the next special or annual shareholders meeting. IND. CODE ANN. § 23-1-42-7(c). In this case, DCA neither filed a statement nor requested a special meeting.

The Control Share Chapter applies to all control share acquisitions of the stock of covered Indiana corporations, regardless of the State of residency of the acquiring person. Similarly, the statute applies regardless whether the shares are acquired (a) in intrastate or interstate commerce, or (b) through a tender offer, open market or private purchases, gift, inheritance, or otherwise.

[3] The District Court and the Seventh Circuit mistakenly thought that IND. CODE ANN. § 23-1-42-9(b)(1) required DCA also to obtain approval by a majority of *all* CTS shares, including "interested shares." Section 9(b)(1) applies only where the proposed acquisition would effect certain changes in the capital structure of the company, such as changing the number of shares of stock, creating a new class of shares, or altering the rights of a class of shares. *See* IND. CODE ANN. § 23-1-38-4(a). The State of Indiana, as intervenor-appellant, brought the district court's error to the Seventh Circuit's attention, but the Court of Appeals repeated the error without explanation.

C. Proceedings In The Courts Below.

On March 10, 1986, DCA filed this action in the District Court, originally against CTS and three of its directors, alleging claims unrelated to this appeal.[4] On April 3, DCA was granted leave to file a third amended complaint adding as Count VIII a claim alleging that the Control Share Chapter is unconstitutional under (a) the Supremacy Clause because allegedly preempted by the Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) ("Williams Act"); and (b) the Commerce Clause. On April 9, 1986, the District Court issued a Memorandum Opinion and Order "grant[ing] DCA's motion for declaratory relief on Count VIII of the third amended complaint" and ruling that the Control Share Chapter, as applied to DCA's specific plans, was preempted by the Williams Act. Appendix at A29.[5] After CTS moved the District Court to certify its judgment on Count VIII as a final and appealable judgment pursuant to Fed. R. Civ. P. 54(b), the District Court *sua sponte* issued a second Memorandum Opinion and Order on April 16, 1986, which (a) stated that, if the Indiana Attorney General had been notified of the constitutional issues pursuant to 28 U.S.C. § 2403(b), the

[4] DCA's original complaint alleged an "illegal proxy scheme" in violation of the Federal securities laws, claiming that CTS's communications to its shareholders were "designed" to "jump the gun" on the April 25, 1986, shareholders' meeting and "to condition the CTS shareholders" to vote to retain the present board of directors. Through March 27, DCA filed two amended complaints alleging additional claims and adding director defendants; CTS filed an answer and counterclaim; and the District Court denied DCA's motion for a temporary restraining order on its original claim. These matters are not involved in the instant appeal.

[5] As well as opposing DCA's constitutional claims on the merits, CTS had objected to any immediate decision on the constitutional issues because, *inter alia,* the Attorney General of Indiana had not been notified of the claim as required by 28 U.S.C. § 2403(b); no opportunity for an evidentiary hearing had been afforded; and CTS's time to answer the third amended complaint had not even run.

District Court would also have held the State statute unconstitutional under the Commerce Clause; (b) certified the court's judgment on Count VIII pursuant to Rule 54(b); and (c) "certified the appeal" of the judgment on Count VIII to the Indiana Attorney General. Appendix at A88.

CTS's appeal to the Seventh Circuit pursuant to 28 U.S.C. § 1291[6] was expedited in view of the imminent Annual Meeting. On April 23, 1986, the Seventh Circuit issued both its judgment affirming the District Court and an order briefly describing its action, stating that a full opinion would issue later. Appendix at A126, A129. On June 9, 1986, the Seventh Circuit issued its final opinion, holding, *inter alia,* that the Indiana Control Share Chapter is unconstitutional both on Supremacy Clause grounds (broader than those recited by the District Court) and under the Commerce Clause.[7]

[6] The Seventh Circuit's opinion, like its original order, erroneously states that the appeal in No. 86-1601 was taken pursuant to 28 U.S.C. § 1292(a)(1) (appeal of grant or denial of preliminary injunction). Appendix at A2, A130. On April 17, 1986, the day following its second opinion on the constitutional claim and Rule 54(b) certification of its judgment on Count VIII, the District Court had entered a preliminary injunction against CTS on DCA's separate State law claim involving a shareholder rights plan promulgated by the CTS board of directors, and denied CTS's motion for a preliminary injunction against DCA based on alleged Federal securities law violations. CTS then separately appealed those District Court rulings in No. 86-1608, and the two appeals were consolidated by the Seventh Circuit. The appeal of the District Court's orders on the preliminary injunction motions (involving issues not presented to this Court) was pursuant to 28 U.S.C. § 1292(a)(1); however, the appeal of the constitutional issues presented here was from the District Court's final judgment on Count VIII, Appendix at A138, and therefore pursuant to 28 U.S.C. § 1291.

[7] The following matters, while not appearing in the appellate record before the Seventh Circuit in the instant appeal, have transpired since the Seventh Circuit's judgment:

(1) On April 24, 1986, DCA purchased one million shares of CTS stock pursuant to its tender offer and now owns approxi-

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THE QUESTIONS ARE SUBSTANTIAL

Though this case arises amid a continuing policy debate about the economic, political, and social effects of hostile takeovers,[8] resolving that debate is not what this case is about. Nor is the issue the extent to which the States have continuing authority to regulate the purchase and sale of shares — the subject matter of the Williams Act. Rather, the heart of this case is whether Federal law bars the States from developing their generic corporation laws in ways that do *not* restrict or regulate the purchase or sale of securities or any other transaction in interstate commerce, but that may (depending on the intentions of a potential bidder) make a State's domestic corporations less attractive as hostile takeover targets.

The Seventh Circuit's decision strikes down on Supremacy and Commerce Clause grounds an Indiana statute that regu-

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mately 27.5% of its outstanding stock, thereby triggering the terms of the Control Share Chapter.

(2) The CTS Annual Meeting was rescheduled and held on May 16, 1986. All of DCA's shares were voted at the meeting, in violation of the Indiana statute but as required by the Seventh Circuit's decision. Nevertheless, DCA's proxy contest was unsuccessful and CTS's incumbent board of directors was re-elected as determined by the count of an independent auditor. DCA has filed new claims, now pending in the District Court, seeking to overturn the results of the election.

(3) DCA's motion for a preliminary injunction against enforcement of a second shareholders' rights plan promulgated by the CTS board was denied by the District Court, and DCA's appeal on that issue is now pending before the Seventh Circuit.

The continuing litigation in the lower courts does not involve the constitutional issues presented by this appeal and could not moot the continuing controversy over DCA's legal authority to vote its recently-acquired shares for all future purposes.

[8] *Compare, e.g.*, Bebchuck, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693 (1985), *with* Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981).

lates *only* the voting rights of shareholders. The statute applies to *all* changes in control of covered Indiana corporations, regardless whether the control shares are acquired in interstate or intrastate commerce, and regardless whether the acquisition is made through a tender offer, open market or private purchases, gift, or any other means. The Indiana statute is *not* an anti-takeover statute directed to the subjects regulated by the Federal securities laws. It does not prohibit or regulate the purchase of shares; nor does it discriminate against interstate commerce or out-of-State residents. Nonetheless, the Seventh Circuit reasoned, in essence, that the statute is unconstitutional simply because it may make Indiana corporations less desirable as takeover targets.

In recent years, this Court has twice noted probable jurisdiction of appeals in cases striking down traditional State anti-takeover statutes on Supremacy and Commerce Clause grounds. *Edgar v. MITE Corp.*, 457 U.S. 624 (1982); *LeRoy v. Great Western United Corp.*, 443 U.S. 173 (1979). *LeRoy* was decided on venue grounds without reaching the constitutional issues. *MITE* reached but did not definitively resolve the issues. Four Justices (one of whom, Justice Powell, also thought the case was moot) joined in one half of Justice White's Commerce Clause opinion. Two Justices joined Justice White's preemption analysis, two others disagreed, and four did not address the issue. Justices Powell and Stevens concurred in the judgment but stated that the decision left room for State legislation that might deter hostile takeovers.

Not surprisingly, decisions in the lower courts after *MITE* reflect considerable uncertainty about the constitutional principles applicable even to State statutes that — unlike the Indiana statute here — *do* regulate tender offers and the purchase of shares. For example, in *National City Lines, Inc. v. LLC Corp.*, 687 F.2d 1122, 1128-33 (8th Cir. 1982), the Eighth Circuit treated as controlling both the Supremacy and Commerce Clause portions of Justice White's opinion in *MITE*, and invalidated a Missouri statute regulating disclosures by a tender

offeror. However, in *Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906, 913 (8th Cir. 1984), the same court noted the divisions in *MITE* — stating that "the [Supreme] Court has not definitively resolved whether the view of Justices Powell and Stevens, the view of Justices White, Burger and Blackmun, or some other analysis should apply" — and upheld a Minnesota statute regulating disclosures by a tender offeror. Similarly, in *Agency Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029, 1034, 1036 (1st Cir. 1982), the First Circuit described the divided opinions in *MITE*, upheld Massachusetts' regulation of "creeping" tender offers against a Supremacy Clause challenge, and rejected the notion that *MITE* stands for a "broad preemption principle under which any state regulation of tender offers would have to be invalidated."

In *L.P. Acquisition Co. v. Tyson*, 772 F.2d 201 (6th Cir. 1985), the Sixth Circuit took a different approach in holding that *MITE* did not invalidate the Michigan Takeover Act. The court relied on Justice Powell's concurrence — specifically, his statement that Justice White's Commerce Clause reasoning "leaves some room for state regulation of tender offers," and his observations about the "adverse consequences in terms of general public interest when corporate headquarters are moved from a city and state." 772 F.2d at 201 (quoting 457 U.S. at 646). Yet the same court had earlier held the same Michigan act to be unconstitutional as applied to an interstate tender offer in *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d 558, 567-68 (6th Cir. 1982).[9]

Thus, even if this case were only *MITE* revisited, it would deserve plenary consideration to resolve the open issues and

[9] *See also Fleet Aerospace Corp. v. Holderman*, FED. SEC. L. REP. (CCH) ¶ 92, 800 (6th Cir. June 25, 1986) (extending Justice White's opinion in *MITE* to invalidate State law subjecting control share *purchases*, not voting rights, to shareholder approval); *Icahn v. Blunt*, 612 F.Supp. 1400, 1414-20 (W.D. Mo. 1985) (same); *APL Limited Partnership v. Van Dusen Air, Inc.*, 622 F. Supp. 1216, 1220-24 (D. Minn. 1985) (same), *vacated on other grounds and appeal dismissed*, Nos. 85-5285/5286-MN (8th Cir. Nov. 26, 1985).

guide the lower courts. In this case, however, the Seventh Circuit extended Justice White's opinion to strike down a statute radically different from the Illinois statute in *MITE*. The Seventh Circuit's invalidation of a statute that does not regulate disclosures to shareholders or the purchase of shares in tender offers is unprecedented and has no logical stopping point. Under its reasoning, every aspect of every State's corporation law — including the composition and election of boards of directors, voting rights of different classes of shares, and requirements of shareholder approval of fundamental corporate events such as mergers, sales of assets, or dissolutions — is subject to constitutional challenge. Any such law may "interfere" with tender offers, in the sense relied upon by the Seventh Circuit, simply by making a corporation a less desirable target than it might be under some alternative set of legal rules.

The Seventh Circuit thus decided important and far-reaching questions of constitutional law in an area where this Court's earlier decisions offer little direct guidance, let alone controlling precedent. Moreover, the nature of tender offer litigation requires the lower courts to decide important constitutional issues under extreme time pressure, as occurred here, and such cases frequently become moot long before this Court can review them. This case therefore deserves plenary consideration both to resolve the issues left unresolved by *MITE* and to decide whether *MITE* extends to invalidate any State corporation law that might adversely affect a hostile takeover.

I. THE CONTROL SHARE CHAPTER DOES NOT CONFLICT WITH THE WILLIAMS ACT IN VIOLATION OF THE SUPREMACY CLAUSE.

The Seventh Circuit's opinion on Williams Act preemption rests on two essential premises. The first is that the Williams Act implicitly requires the States to maintain a policy of "neutrality" in tender offers, and thus preempts State statutes that do not actually conflict with Federal statutory provisions

but may nonetheless "favor" one side or the other in the contest. That proposition was accepted by three Justices in *MITE*, rejected by two others, and not addressed by the remaining four. The second premise is that this policy of "neutrality" extends beyond the scope of matters regulated by the Williams Act itself — disclosures to shareholders and the purchase and sale of shares — to other State corporation laws that may affect the desirability of a tender offer. The decision of the Seventh Circuit thus "Federalizes" State corporation law to the extent that any State law may, by some uncertain standard, "unduly" affect the desirability or outcome of either a tender offer itself or a tender offeror's post-acquisition plans for the target. Neither Justice White in *MITE* nor any lower court decision, before this one, has gone so far in extending Federal law into the internal affairs of corporations created by the States' own laws.

A. The Control Share Chapter is Entitled to a Strong Presumption of Constitutionality.

The ordinary presumption of constitutionality given to State laws is strongest in the preemption context. To preserve the States' lawmaking authority, the starting assumption is "that Congress did not intend to displace state law," *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981), and preemption is disfavored "in the absence of persuasive reasons — either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained." *Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311, 317 (1981).

Because the Control Share Chapter deals only with the post-acquisition voting rights of shares in a potentially fundamental event for the corporation and its other shareholders — a change in control — the presumption against preemption is especially strong. "Where . . . the field that Congress is said to have pre-empted has been traditionally occupied by the States, 'we start with the assumption that the historic police powers of the States were not to be superseded

by the Federal Act unless that was the *clear and manifest* purpose of Congress.'" *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977) (emphasis added) (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)). Here, the Seventh Circuit held preempted a law directly governing the internal affairs of corporations and the voting rights of shareholders — historically matters of *exclusive* State concern.

B. The Provisions of the Williams Act Do Not Preempt State Law in the Absence of a Direct Conflict With Federal Law.

The Williams Act added to the Securities Exchange Act of 1934 ("Exchange Act") sections 13(d), 13(e), 14(d), 14(e), and 14(f). The Williams Act governs disclosures and statements in connection with offers to purchase shares, Exchange Act §§ 13(d), 14(d), 14(e) & 14(f); requires or prohibits certain acts so that investors will have sufficient time to decide whether to tender their shares, *id.* §§ 13(e) & 14(d); and imposes substantive requirements on tender offerors' purchases of shares, *id.* § 14(d).

None of these statutory provisions expresses *any* limit on State authority. Instead, all are subject to Section 28(a) of the Exchange Act, which states that the Act does not preempt State law that does not actually "conflict with" the "provisions" — not the *policy* — of the Exchange Act. 15 U.S.C. § 78bb(a). Thus the only *statutory* expression of Congressional intent is that the Williams Act is not intended to displace State regulation of tender offers in the absence of a *direct* conflict.

C. The Legislative History of the Williams Act Does Not Support Preemption of State Laws That May Impede Takeovers.

The Seventh Circuit did not base its preemption holding on any direct conflict.[10] Rather, it concluded from only the legisla-

[10] The closest the Seventh Circuit came to identifying a "conflict" was its claim that, because the disinterested shareholder vote on the

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tive history of the Williams Act that Congress had "struck a delicate balance between the contending factions in the takeover controversy," and had implicitly prohibited the States from taking any steps that might tip that balance. Appendix at A23.

This Court's decision in *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 26-35 (1977), explained the context of the Congressional "balance" — a context the Seventh Circuit ignored. As the *Piper* Court observed, the bill as first introduced was intended to protect incumbent corporate management from cash tender offers, a strategy that had not previously been regulated by Federal securities laws. In committee hearings, however, witnesses "indicated that takeover bids could often serve a useful function." *Id.* at 30. Sensitive to the suggestion that the bill would favor one side or the other in control contests, the Williams Act sponsors "made it clear that the legislation was designed solely to get needed information to the investor," *id.* at 30-31, and that they had "taken extreme care to avoid tipping the scales either in favor of management or in favor of the person making the takeover bid." *Id.* at 31

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voting power of control shares might not take place until 50 days after filing of an optional acquiring person statement, *see* IND. CODE ANN. § 23-1-42-7(b), a tender offeror would in practice wait beyond the 20 business day (*circa* 28 calendar day) *minimum* Williams Act waiting period before purchasing shares — which the Seventh Circuit characterized as "impos[ing] a 50-day delay on tender offers." Appendix at A20. The characterization is inaccurate. There is in fact no legally cognizable "conflict," since the shareholder vote under the Indiana law has *no* impact whatever on the acquirer's legal right to buy shares in a tender offer. *See infra* at 17-18. By speculating about the statute's possible impact on a tender offeror's practical calculations, the lower court substituted economic theorizing for the proper focus of judicial inquiry under the Supremacy and Commerce Clauses — namely, whether the States (whatever the possible *economic* impact of their decisions) have the constitutional *authority* to regulate in a given area. *See infra* at 25-28.

(quoting 113 Cong. Rec. 24664 (1967) (remarks of Sen. Williams)).

Placed in context, the isolated references to neutrality on the part of *Congress* do not support the Seventh Circuit's conclusion (and Justice White's in *MITE*) that the Williams Act also implicitly barred the *States* from affecting the "balance of power" between the tender offeror and the target:

> Congress was indeed committed to a policy of neutrality in contests for control, but its policy of evenhandedness does not go either to the purpose of the legislation or to whether a private cause of action is implicit in the statute. Neutrality is, rather, but one characteristic of legislation directed toward a different purpose — the protection of investors. Indeed, the statements concerning the need for Congress to maintain a neutral posture in takeover attempts are contained in the section of the Senate Report entitled, "Protection of Investors." Taken in their totality, these statements confirm that what Congress had in mind was the protection of shareholders, the "pawn[s] in a form of industrial warfare." The Senate Report expressed the purpose as "plac[ing] investors on an equal footing with the takeover bidder," Senate Report 4, without favoring either the tender offeror or existing management.

430 U.S. at 29-30. Thus, the references to "neutrality" suggest only that Congress *itself* did not wish to "tip the balance" with the Williams Act, not that Congress implicitly intended the Act to be a comprehensive scheme regulating tender offers to the exclusion of State authority.

The Seventh Circuit acknowledged that "it is a big leap from saying that the Williams Act does not itself exhibit much hostility to tender offers to saying that it implicitly forbids states to adopt more hostile regulations." Appendix at A22. Nonetheless, it relied on Justice White's and its own opinions in *MITE* and on subsequent lower court decisions to justify that "big leap," saying that "whatever doubts . . . we might entertain as an original matter are stilled by the weight of precedent." Appendix at A23. The "weight of precedent" is not at all persuasive here, however, because a majority of this Court has

never accepted the proposition that the Williams Act forbids States from adopting any laws more hostile to takeovers. Indeed, Justices Powell and Stevens both rejected the suggestion that Congressional neutrality was tantamount to Federal prohibition of more restrictive State laws. 457 U.S. at 647, 655.

The Seventh Circuit's reliance on *Piper* and *Schreiber v. Burlington Northern, Inc.*, 472 U.S. ____, 105 S. Ct. 2458, 2463, 86 L. Ed. 2d 1 (1985), is clearly misplaced. In *Piper*, this Court expressly *rejected* the argument that the Williams Act created a "pervasive scheme of federal regulation of tender offers" that would support an implied cause of action (or, necessarily, preemption of State law). 430 U.S. at 29. In *Schreiber*, this Court *refused* to extend the Williams Act to regulate the defensive strategies of the target board of directors, leaving such matters to State corporation law. There was no suggestion in *Schreiber* that the State corporation law governing defensive strategies must also display an appropriate "neutrality" lest it encroach upon the Williams Act; yet that result is logically compelled by the Seventh Circuit's decision.

D. Any Preemption Under the "Neutrality Principle" is Limited to the Subject Matter of the Williams Act and Does Not Preempt State Corporation Laws Protecting Remaining Shareholders Caught in Fundamental Changes in the Corporation.

Even assuming that the "neutrality" statements in the legislative history can preempt otherwise valid State laws, it still does not follow — as the Seventh Circuit effectively held — that *any* State laws making tender offers less attractive to the offeror are preempted. Rather, the scope of any preemption arising from this legislative history must be limited by the subject matter of the Williams Act.

This Court's cases have necessarily limited preemption to those matters *actually regulated* by Federal statutes, not to any State law that might touch on the area. In *Huron Portland Cement Co. v. Detroit*, 362 U.S. 440, 445-46 (1966), for

example, the Court concluded that Federal laws for inspection of steamship boilers did not preempt local air pollution regulations even though the local laws prohibited conduct allowed by Federal law. Because there was "no overlap" between the Federal and local laws, there was no preemption. "To hold otherwise would be to ignore the teaching of this Court's decisions which enjoin seeking out conflicts between state and federal regulation where none clearly exists." 362 U.S. at 446. *Accord, Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 237 (1947).

The Williams Act and its legislative history address only a narrow subject — the interactions among tender offerors, incumbent management, and investors up to the point when the investor makes an "informed choice" whether to tender his shares. As Justice White said in *MITE*, "Congress sought to protect the investor not only by furnishing him with the necessary information but also by withholding from management or the bidder any undue advantage that could frustrate the exercise of an informed choice." 457 U.S. at 634. The Control Share Chapter regulates only post-acquisition voting rights and addresses entirely different concerns, namely, protecting the interests of other shareholders (*e.g.*, in a tender offer, those who choose *not* to tender their shares) vis-a-vis a new and potentially dominant one. The Chapter is thus beyond the scope of whatever preemption might be mandated by the supposed "neutrality principle."

The Indiana legislature had legitimate reasons to be concerned with the situation where one shareholder acquires a dominant portion of voting shares. There is an inherent possibility of unfair treatment when a dominant (but not 100 percent) shareholder maintains the controlled corporation as a partly-owned subsidiary for some unspecified time. *See* Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693, 1711 (1985) (dominant shareholder adopts such a strategy only to take

"advantage of minority shareholders"). The Indiana Control Share Chapter allows dispersed shareholders in a firm with a new and potentially dominant shareholder to protect their interests by voting.

In so doing, the Chapter reflects a valid legislative concern for shareholder control over a fundamental event in the corporation's existence — the transformation of the corporation from a collection of dispersed shareholders to one dominated by a single shareholder. If there is no shareholder vote and the dominant shareholder gains control of the board, the large group of remaining shareholders, "without its consent, is participating in a different enterprise as certainly as if there had been a merger with a third party." Brudney, *Equal Treatment of Shareholders*, 71 CAL. L. REV. 1072, 1122 (1983). In this respect, the Control Share Chapter is squarely in the tradition of State corporation laws requiring shareholder votes on other fundamental corporate events such as mergers, sales of assets, changes in voting power of classes of shares, or dissolutions.

But whatever the substantive merits of the policy decisions reflected in the Control Share Chapter, those decisions were Indiana's to make. In view of the narrow subjects regulated by the Williams Act, there is no basis for concluding that *Congress* has made a policy judgment to bar innovative State statutes governing the voting power of shares in State-created corporations. Congress has instead traditionally left regulation of these internal corporate affairs to the State of incorporation. *Cort v. Ash*, 422 U.S. 66, 84 (1975). Indeed, the established validity of State authority to govern the internal affairs of corporations has led this Court to construe the Exchange Act narrowly so as *not* to "federalize . . . the law of corporations." *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977). *Accord, Schreiber v. Burlington Northern, Inc.*, 472 U.S. ___, 105 S. Ct. 2458, 86 L. Ed. 2d 1 (1985) (§ 14(e) does not apply

to alleged breaches of fiduciary duty by incumbent board of directors in tender offer context).[11]

The decision below violates that principle, and its necessary implications highlight the need for review by this Court. The list of State laws that could be preempted under the Seventh Circuit's analysis is remarkably long. The Model Business Corporation Act — followed by many States — has long authorized directors to determine the relative voting rights of classes and series of shares, which can obviously be used to discourage a tender offer. *See* MODEL BUS. CORP. ACT § 16 (1969); REV. MODEL BUS. CORP. ACT §§ 6.01(c), 6.02(1984). Statutes requiring shareholder votes on fundamental corporate events — *e.g.*, mergers, IND. CODE. ANN. § 23-1-40-3, sales of of assets, IND. CODE ANN. § 23-1-41-2, and dissolutions, IND. CODE ANN. § 23-1-45-1 — could certainly interfere with a tender offeror's desired takeover scheme and thus be preempted. State laws governing the timing of shareholder meetings, *e.g.*, IND. CODE ANN. §§ 23-1-29-1 *et seq.*, or the election of directors, *e.g.*, IND. CODE ANN. §§ 23-1-33-1 *et seq.*, may affect a tender offeror's ability to take control of a target corporation and thus also become constitutionally suspect.

Even assuming, then, that the "neutrality" observations in the legislative history have preemptive force, that force is limited to the subjects actually regulated by the Williams Act. That subject matter at least provides a baseline by which courts may determine whether State statutes are "neutral" or not. But outside that limited context, the "neutrality" observations do not give the Federal courts a roving mandate to adjudicate the

[11] Indeed, in 1984 Congress rejected proposed legislation that would have restricted defensive tactics in takeover contests, H.R. 5693, 98th Cong., 2d Sess. (Comm. Print 1984), in part because the bill would have intruded on State corporation law. *See Annual Review of Federal Securities Regulation*, 40 BUS. LAW. 997, 1019-21 (1985). *See also* H.R. Rep. No. 1028, 98th Cong., 2d Sess. 9-17 (1984) (noting that *Congress* must address proper relationship between State and Federal law in regulating takeovers).

"neutrality" of all State corporation laws that may affect the desirability of tender offers.

II. THE CONTROL SHARE CHAPTER DOES NOT VIOLATE THE COMMERCE CLAUSE.

The Control Share Chapter does not discriminate in any way against interstate commerce or out-of-State residents, and it applies only to Indiana corporations that also have other substantial ties to the State. Nor does the statute prohibit or regulate purchases of shares, whether in interstate commerce or otherwise. Instead, it regulates only the post-acquisition voting rights of control shares, however acquired. By holding that the Control Share Chapter violates the Commerce Clause, the Seventh Circuit extended the reach of the "dormant" Commerce Clause too far into the States' traditional regulation of the internal affairs of the corporations they create.

The Chapter serves the legitimate State purpose of protecting the interests of remaining shareholders who may be adversely affected by a change in control of the corporation. Any indirect effects of the Chapter on interstate commerce are minor, especially since State law exclusively creates and defines the stock rights that are available for purchase in the first place. The Commerce Clause does *not* require State law to *define* shareholders' rights (or any other property rights) in any specific way, so long as the State does not discriminate against interstate commerce. The Seventh Circuit's holding to the contrary is unprecedented in Commerce Clause jurisprudence.

A. The Control Share Chapter Does Not Directly Regulate or Discriminate Against Interestate Commerce.

The first critical feature of the Control Share Chapter is that it neither regulates nor discriminates against interstate commerce. The State's regulation of the voting rights of control shares applies whether the control shares are acquired in intrastate or interstate commerce, and whether through a tender offer, private or open market purchases, inheritance, or otherwise. Likewise, it applies regardless of the residences of the buyer and seller.

The Chapter therefore easily passes the most basic of Commerce Clause tests. This Court accords "special deference" to State laws that do not discriminate against interstate commerce, based on the sound assumption that where the law's "burden usually falls on local economic interests as well as other States' economic interests, [this ensures] that a State's own political processes will serve as a check against unduly burdensome regulations." *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 675 (1981) (plurality opinion).[12] *Accord, Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, 125-26 (1978) (no discrimination even where burden fell only on out-of-State businesses); *Huron Portland Cement Co. v. Detroit,* 362 U.S. 440, 448 (1960) (no discrimination).

B. The Control Share Chapter Applies Only to Indiana Corporations And Poses No Risk Of Multiple Burdens.

The second critical feature of the Control Share Chapter for Commerce Clause purposes is that it applies only to Indiana corporations with additional ties to the State.[13] Therefore, in addition to being nondiscriminatory, it poses no risk of subjecting the corporation or a tender offeror to cumulative, multiple and inconsistent State regulations—the other major concern in Commerce Clause jurisprudence. In *MITE,* for example, the

[12] The plurality in *Kassel* concluded that this traditional deference was weakened where the State also created several exemptions that clearly reduced the burden of the regulations on its own residents. 450 U.S. at 676-78. The Indiana Control Share Chapter contains no such discriminatory exemptions.

[13] The corporation must also have (a) its principal place of business, its principal office, or substantial assets in the State, and (b) either 10% of its shareholders in Indiana, 10% of its shares owned by Indiana residents, or 10,000 shareholders in Indiana. IND. CODE ANN. § 23-1-42-4(a).

Illinois statute, which prohibited stock purchases and sales in a tender offer, was not so limited, and Justice White's opinion noted that "if Illinois may impose such regulations, so may other States; and interstate commerce in securities transactions generated by tender offers would be thoroughly stifled." 457 U.S. at 642. *Huron Cement* made the same point: "State regulation, based on the police power, which does not discriminate against interstate commerce *or operate to disrupt its required uniformity,* may constitutionally stand." 362 U.S. at 448 (emphasis added). In this case there is obviously no need for national uniformity in shareholder voting rights (unlike, for example, railroad or trucking regulation), and no risk of overlapping and inconsistent State regulation.

The absence of both discrimination against interstate commerce and any risk of overlapping and inconsistent State regulations should dispose of the Commerce Clause issue here. *See Huron Cement,* 362 U.S. at 448. Despite various formulations of the test, this Court has *never* struck down on Commerce Clause grounds State legislation that did not exhibit at least one of these features.

C. The Control Share Chapter Serves Legitimate State Interests in Protecting Non-Dominant Shareholders in Indiana Corporations.

In *Pike v. Bruce Church, Inc.,* 397 U.S. 137, 142 (1970), this Court articulated a balancing test for "evenhanded" regulations "affecting" interstate commerce:

> Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits.

Assuming *arguendo* that (even absent discrimination or threat of multiple burdens) the *Pike* test applies here at all, the balance of interests is heavily in favor of the State statute.

The Control Share Chapter protects non-dominant shareholders in Indiana corporations whose interests could be ad-

versely affected by a change in control of the corporation. By permitting these shareholders to decide whether voting control of the corporation should change hands through acquisition of the control shares by a single dominant person, the Chapter serves the legitimate State purpose of protecting their interests and promoting shareholder control over fundamental changes in the corporation. As discussed at greater length earlier in addressing the Supremacy Clause issue, minority or dispersed shareholders are vulnerable to exploitation by a dominant shareholder.

Indiana, like its sister States, has commonly required shareholder approval of fundamental changes in corporate affairs, and the new Indiana Business Corporation Law continues that practice. *See, e.g.,* Ind. Code Ann. §§ 23-1-38-3 (amendments to articles of incorporation); 23-1-40-3 (mergers and share exchanges); 23-1-41-2 (disposition of substantial assets); and 23-1-45-2 (dissolution). The Control Share Chapter's requirement of a disinterested shareholder vote reflects the Indiana legislature's conclusion that a single dominant shareholder's acquisition of a substantial block of shares is also a fundamental change for the corporation and should also be subject to shareholder approval. The legislature's judgment should not be second-guessed by the courts when the statute neither discriminates against interstate commerce nor regulates an interstate purchase in the first place.

The Seventh Circuit dismissed Indiana's interests as "trivial or even negative" by saying that "Indiana has no interest in protecting residents of Connecticut from being stampeded to tender their shares to Dynamics at $43." Appendix at A25 (citing *MITE*). That analysis ignores both the far different context of *MITE* and the State's real interests in the case at bar. The statute at issue here is *not* designed to protect shareholders — whether Indiana residents or not — in deciding whether to *sell* their shares, and it has utterly no effect on their ability to do so. Rather, the Control Share Chapter is intended to protect

shareholders — both resident and nonresident — of Indiana corporations who decide *not* to tender or otherwise dispose of their shares.

The Seventh Circuit's reasoning also misreads Justice White's opinion in *MITE*, apparently relying on the following passage:

> While protecting local investors is plainly a legitimate state objective, the State has no legitimate interest in protecting nonresident shareholders. Insofar as the Illinois law burdens out-of-state transactions, there is nothing to be weighed in the balance to sustain the law.

457 U.S. at 644. That statement in *MITE* dealt with a statute that was *not* limited to Illinois corporations and that *did* regulate purchases and sales of shares between out-of-State sellers and buyers. Indiana, however, has a legitimate interest in protecting *all* shareholders of *Indiana* corporations in their relationships *inter sese*. The State is entitled to take steps to protect the investments of nonresidents as well as residents. That is a legitimate interest that necessarily inheres, in one form or another, in every State's corporation code.[14]

D. Any "Effects" of the Control Share Chapter on Interstate Commerce Do Not Burden Such Commerce and Do Not Rise to Constitutional Significance.

Assuming that the *Pike* balancing test even applies here, the Control Share Chapter could violate the Commerce Clause only if it imposed a burden on interstate commerce that is "clearly excessive" in relation to the State's interest in protecting non-dominant shareholders. The Seventh Circuit recognized that the Control Share Chapter does not impede interstate commerce in equity securities. The heart of its Commerce

[14] Indeed, if Indiana law *discriminated* between voting rights of resident and nonresident shareholders, it would create (rather than avoid) constitutional problems. *See Supreme Court of New Hampshire v. Piper*, 84 L. Ed. 2d 205, 210-11 (1985); *Toomer v. Witsell*, 334 U.S. 385, 396 (1945).

Clause analysis was its judgment (based on *no* evidence) that the Chapter impedes "commerce in corporate control" that the Seventh Circuit deemed "important." Appendix at A26. The Seventh Circuit reasoned that the efficiency with which a corporation's assets are employed "depends on the market for corporate control — an interstate, indeed international, market that the State of Indiana is not authorized to opt out of, as in effect it has done in this statute." *Id.* Of course, this *ipse dixit* is simply wrong. Nothing in the Commerce Clause requires the States to create corporations at all, much less — as the Seventh Circuit held — to define the rights of shareholders so as to tie the voting rights of a share inextricably to an equity interest in the corporation's profits and property.

The Seventh Circuit made two fundamental errors. First, Judge Posner's opinion mistakenly equates economic efficiency with constitutionality. This Court's decision in *Exxon* makes clear that a State may impose "inefficient" regulations on commerce in order to further other goals, such as fairness to all shareholders. In *Exxon*, the fact that a State law altered "the natural functioning of the interstate market" was unimportant because the Commerce Clause does not protect "the particular structure or methods of operation" in a market. 437 U.S. at 127. Maryland was entitled to protect independent service station operators, even if that was not "efficient." The Seventh Circuit's concern about the efficient use of corporate assets here — like the plaintiffs' argument in *Exxon* — "relates to the wisdom of the statute, not to its burden on commerce." 437 U.S. at 128. The efficiency argument should therefore be addressed by the Indiana legislature, not the Federal courts.

Equally important, Judge Posner's reasoning fails to realize that the "market for corporate control" is a market *created only by State law defining property rights and ownership interests.* The market exists only because Indiana and other States have enacted laws that create corporations in the first place, and then permit them to issue equity securities that may then in turn be bought and sold. As Chief Justice Marshall explained long ago:

> A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence.

Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819). State law defines the terms of the contract among the corporation, its shareholders and the State, and thereby (as is true of all State-created property interests) defines any interest that is available for sale, whether in interstate commerce or otherwise.

There is no basis for the Seventh Circuit's holding that the Commerce Clause requires Indiana to link voting rights inseparably to an equity interest in a company. The State may, in exchange for the privileges of the corporate franchise, impose conditions on those privileges, including limits on the transfer of voting power, which do not discriminate against interstate commerce. The fact that DCA made its purchases in interstate commerce adds nothing to its claim. "A man cannot acquire a right to property by his desire to use it in commerce among the states. Neither can he enlarge his otherwise limited and qualified right to the same end." *Hudson County Water Co. v. McCarter*, 209 U.S. 349, 357 (1908) (Holmes, J.). Thus, the fact that DCA's stock purchases were across State lines here — like the fact that interstate businesses were required to divest property in *Exxon* — is irrelevant for Commerce Clause analysis. 437 U.S. at 125.

While there may currently exist, as a practical matter, a familiar interstate market in corporate control, Indiana has simply chosen to give shareholders of its domestic corporations new rights vis-a-vis potentially dominant new shareholders. The Seventh Circuit found this unsettling, but it overlooked that:

> A Constitution is not intended to embody a particular economic theory, whether of paternalism and the organic

> relation of the citizen to the state or of *laissez faire*. It is made for people of fundamentally differing views, and the accident of our finding certain opinions natural and familiar, or novel, and even shocking, ought not to conclude our judgment upon the question whether statutes embodying them conflict with the Constitution of the United States.

Lochner v. New York, 198 U.S. 45, 75-76 (1905) (Holmes, J., dissenting). This Court's decision in *Exxon* makes clear that the Commerce Clause does not require the States to establish economically "efficient" markets, even where interstate commerce is in some sense "affected." However familiar such markets may be, the Commerce Clause does not protect their "particular structure or methods of operation." 437 U.S. at 127. *See* L. TRIBE, AMERICAN CONSTITUTIONAL LAW 25 (Supp. 1979) (discussing *Exxon*); *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) ("It is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country").[15]

The Seventh Circuit's disregard of these fundamental principles of Federalism — and its substitution of economic analysis for Commerce Clause jurisprudence — are highlighted by its twin statements that the fact "that the mode of [State] regulation involves jiggering with voting rights cannot take it outside the scope of [Federal] judicial review," and that any other conclusion would invite "facile evasions" of the Commerce Clause. Appendix at A27. Both statements are wrong. The Commerce Clause (like the Constitution generally) is precisely concerned with which "modes" of regulation are the

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[15] Moreover, any risks posed by the Control Share Chapter are risks for Indiana itself, its domestic corporations, and their shareholders — not to the Nation. If the Seventh Circuit's economic analysis were correct, one might reasonably expect the Control Share Chapter to drive down the market price for shares in Indiana corporations. If that should occur — and whether it would is highly debatable — it would raise no Commerce Clause issue. *See Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 444 n.18 (1978).

province of the Federal Government and which are the province of the States. The proper focus of constitutional inquiry is where the Constitution places the power to act — an inquiry that does not turn on whether regulation will yield a given economic result in a particular case. *Cf. Synar v. United States*, 626 F. Supp. 1374, 1403 (D.D.C.), *aff'd*, 54 U.S.L.W. 5064 (U.S. 1986). The States may not be permitted to restrict, as Illinois sought to do in *MITE*, transactions in interstate commerce regulated by Federal statute — the purchase and sale of securities. That does not mean, however, that a State statute of the kind at issue here — regulating (as the States have traditionally and exclusively done) the voting power of shares of the State's corporations — is invalid simply because one of its effects may be to make the purchase of such shares less attractive as an *economic* proposition for a prospective acquirer. Whether the Commerce Clause is "honored" or "evaded" depends not on whether a given economic outcome is reached, but rather on whether the Federal Government and the States are acting within their respective spheres of constitutional authority.

Moreover, the logic of the Seventh Circuit's contrary reasoning points inexorably in one direction: Any aspect of State corporation law that may make it harder to take over voting control of a domestic corporation violates the Commerce Clause. While the Seventh Circuit "assume[d] without deciding that Indiana has a broad latitude in regulating [the internal affairs of its corporations], even when the consequence may be to make it harder to take over an Indiana corporation," Appendix at A27, its reasoning in fact has no stopping point. It reaches any aspect of State corporate law that may discourage a takeover; the Seventh Circuit articulated no logical distinction between such laws, and none exists. If a State may not "jigger with voting rights," there is no reason why it may "jigger" with schedules and voting methods for electing boards of directors; fiduciary standards applicable to takeover defenses; restrictions on freeze-out mergers that may injure minority shareholders; or

any other aspect of corporation law that may annoy a given tender offeror.

CONCLUSION

Since the Federal constitutional issues here are so substantial, this Court should note probable jurisdiction, set the case for plenary consideration, and reverse the judgment below.

July 21, 1986.

Respectfully submitted,

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86-71 (8)

No.

IN THE

Supreme Court of the United States

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

APPENDIX TO JURISDICTIONAL STATEMENT OF APPELLANT CTS CORPORATION

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In the

United States Court of Appeals

For the Seventh Circuit

Nos. 86-1601, 86-1608

DYNAMICS CORPORATION OF AMERICA,

Plaintiff-Appellee, Counterdefendant-Appellee,

v.

CTS CORPORATION,

Defendant-Appellant, Counterplaintiff-Appellant.

STATE OF INDIANA,

Intervenor-Appellant.

Appeals from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 86 C 1624—**Susan Getzendanner,** ***Judge.***

ARGUED AND DECIDED APRIL 23, 1986—OPINION MAY 28, 1986
AMENDED JUNE 9, 1986

Before BAUER, CUDAHY, and POSNER, *Circuit Judges.*

POSNER, *Circuit Judge.* On March 10 of this year Dynamics Corporation of America, which already owned 9.6 percent of the common stock of CTS Corporation, made a tender offer for another million shares. The offer if accepted would bring its stock holdings up to 27.5 percent of the company. On the same day, Dynamics filed this suit in the federal district court in Chicago; as later amended, the suit sought to enjoin the enforcement of Indiana's statute regulating takeovers, on the ground that

the statute violates the supremacy and commerce clauses of the federal Constitution. When CTS "opted in" to a new Indiana statute on the subject, the Control Share Acquisition Chapter as it is called, Ind. Code §§ 23-1-42-1 *et seq.*, Dynamics further amended its complaint to challenge the new statute on the same grounds. A pendent count in the complaint sought to enjoin CTS from enforcing a recently adopted shareholders' rights plan ("poison pill"), on the ground that it violated the fiduciary obligations of CTS's management toward its shareholders. CTS counterclaimed against Dynamics, seeking an injunction against the tender offer on the grounds that it would result in a violation of section 8 of the Clayton Act, 15 U.S.C. § 19 (interlocking directorates), and that it failed to disclose material information. There are some individual parties, but as they are not important to the legal issues we shall ignore them.

Both Dynamics and CTS moved for preliminary injunctions. After a month of frantic pretrial discovery a one-day evidentiary hearing was held before the district judge, who in a series of orders then ruled that the poison pill plan violated Indiana law, that the Indiana statute violated both the supremacy and commerce clauses of the federal Constitution, and that CTS was not entitled to a preliminary injunction. She therefore granted the preliminary injunction requested by Dynamics. CTS, joined by the Attorney General of Indiana, who has intervened in the case to defend his state's statute, appeals under 28 U.S.C. § 1292 (a)(1), which allows an immediate appeal from an order granting or denying a preliminary injunction. We accelerated our consideration of the appeal because Dynamics had only till April 24 to decide whether to buy the shares tendered in response to its offer. We heard argument on April 23 and later that day affirmed the district judge's orders, with a notation that an opinion explaining the grounds of our decision would follow.

The main issues we must address are the lawfulness of CTS's poison pill scheme, the district court's compliance with a federal statute requiring that a state's attorney general be notified that the constitutionality of a statute

of his state is being challenged, the constitutionality of the new Indiana takeover statute under the supremacy clause and also under the commerce clause, the significance of the potential violation of the Clayton Act, and the adequacy of the disclosures made in the tender offer.

Before taking up these issues we shall comment briefly on the procedural posture of the case in this court, an appeal from orders granting and denying requests for preliminary injunctions. As emphasized in our recent opinions, in different but compatible formulations, the task for a district judge asked to grant a preliminary injunction is to compare the irreparable harm to the plaintiff if the injunction is denied, weighted by the likelihood that the denial would be erroneous because the plaintiff will prevail in the plenary trial, with the irreparable harm to the defendant if the injunction is granted, weighted by the likelihood that the grant would be erroneous because the defendant, not the plaintiff, will prevail in the trial. See *Lawson Products, Inc. v. Avnet, Inc.*, 782 F.2d 1429, 1433-34 (7th Cir. 1986); *American Hospital Supply Corp. v. Hospital Products Ltd.*, 780 F.2d 589, 593 (7th Cir. 1986); *Roland Machinery Co. v. Dresser Industries, Inc.*, 749 F.2d 380, 387-88 (7th Cir. 1984). So, for example, the greater the probability that the plaintiff will win the case in the end, the less irreparable harm he need show relative to the defendant in order to get the preliminary injunction. If both parties are likely to suffer the same amount of irreparable harm, so far as estimation is possible, then likelihood of success becomes decisive. See *American Hospital Supply Corp. v. Hospital Products Ltd., supra*, 780 F.2d at 598. That seems a reasonable description of the present case; the fact that both parties sought preliminary injunctions does not affect the analysis.

If the tender offer is blocked, Dynamics will lose an opportunity that may never recur. The present owners of shares in CTS who have tendered them to Dynamics may lose, too, but their loss is easily quantified—it is the difference between the price in the tender offer and the price to which CTS stock falls. The only problem is uncer-

tainty as to how many shares Dynamics would actually have bought if its offer was oversubscribed, as it was. But, conversely, if the tender offer is not blocked, CTS's shareholders will be irrevocably harmed if, as CTS predicts, they are stampeded into selling their shares to Dynamics for a lower price than the shares would eventually command if the tender offer were defeated, or if shareholders who do not tender are coerced into surrendering their shares later at inadequate prices in a "back-end" deal engineered by a board of directors that Dynamics is expected to control if its tender offer succeeds. The harms are very difficult to quantify and it seems best to treat them as offsetting. Hence Dynamics is entitled to the relief it sought (including the denial of the preliminary injunction sought by CTS) if but only if it is more likely than CTS to prevail at a full trial, in the unlikely event that one is ever held.

When the only issue on appeal from an order granting or denying a request for a preliminary injunction is likelihood of success, the role of the appellate court is little different from that in an appeal from a final judgment. Review of the district judge's legal rulings is plenary, review of the judge's findings of fact limited to clear errors. Since the complex, particularistic, often intuitive process of weighing likelihood of success against the balance of irreparable harms is not involved when that balance is assumed to be even, the deference that we give the district judge's striking of that balance is not a factor in this appeal.

Against this background we first ask whether the district court was right to conclude that the adoption of the poison pill violated the fiduciary obligations of CTS's management to its shareholders. The parties agree both that the question is governed by the common law of Indiana and that Indiana takes its cues in matters of corporation law from the Delaware courts, which are more experienced in such matters since such a large fraction of major corporations is incorporated in Delaware and such a small fraction in Indiana.

The whole issue of permissible defensive tactics in the face of a tender offer is immensely contentious, and it is no business of ours, whose duty on this branch of the appeal is only to predict how the Indiana courts would evaluate CTS's poison pill maneuver, to choose sides. There are two polar positions in the debate. One views hostile takeovers as a bad thing, on a variety of grounds such as that they make managers of companies that are potential targets of takeover bids worry too much about short-term financial results and that they promote absentee ownership and control. See, e.g., Scherer, *Takeovers: Present and Future Dangers*, Brookings Rev. (winter-spring 1986), at 15; Herman, Corporate Control, Corporate Power 100-01 (1981). Whether or not Dynamics ever merges CTS into it, the parties seem agreed that if the tender offer succeeds, Dynamics, as by far the largest shareholder of CTS, will probably be able to elect a majority of the board of directors. Dynamics is a New York corporation with headquarters in Connecticut, CTS an Indiana corporation with headquarters in Indiana. The record is not clear on where the firms' assets and employees are concentrated, and indeed reveals little about the companies except that CTS is a manufacturer of electronic and electromechanical components and Dynamics a diversified manufacturer of consumer and industrial products and that both are large companies whose stock is traded on the New York Stock Exchange.

The other pole is that all resistance to takeover attempts is bad. See, e.g., Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 Harv. L. Rev. 1161 (1981); Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 Stan. L. Rev. 819 (1981); cf. SEC Office of Chief Economist, *A Study on the Economics of Poison Pills*, Fed. Sec. L. Rep. (CCH) ¶ 83,971 (March 5, 1986). The market price of publicly traded stock impounds all available information about the value of the stock, and anyone who offers a higher price (Dynamics' tender offer price was $43, and when the of-

fer was made CTS's stock was trading at $36) thereby offers an unequivocal benefit to the shareholders of the target firm, which management if it is really a fiduciary of the shareholders should embrace rather than oppose. In that way the market for corporate control will be kept fluid and corporate assets will be transferred, with a minimum of friction, to those who value them the most, as measured by the prices they offer. See also Ginsburg & Robinson, *The Case Against Federal Intervention in the Market for Corporate Control*, Brookings Rev. (winter-spring 1986), at 9.

It is a safe prediction that the Indiana courts would reject the polar views, as the Delaware courts have done. To allow management to use its control of the board of directors to frustrate all hostile takeovers would nullify an important protection for shareholders. The threat of hostile takeover plays a vital role in keeping management on its toes. CTS has been a troubled firm of late; a major acquisition (which Dynamics, long a major shareholder, opposed) soured, and was written off at a large loss. If CTS's management is allowed to insulate the company from any change of control to which management does not agree, the shareholders may be unable to realize the potential value of their investment. Maybe under different control, specifically Dynamics' control, CTS would be a more valuable company; then its shareholders would benefit from a takeover, hostile or otherwise. It is only human for CTS's officers and directors to doubt that a company which, if it takes control of CTS, will fire them can actually do a better job of running "their" company. But it is not their company; at least it is not supposed to be. It is supposed to be the shareholders' company, for it is they who are entitled to all the income that the company generates after paying off all contractually or otherwise obligated expenses. The officers and directors are the agents and fiduciaries of the shareholders and owe a duty of complete loyalty which is inconsistent with erecting insuperable barriers to hostile takeovers.

But it does not follow that loyalty requires passivity. See, e.g., Bebchuk, *The Case for Facilitating Competing Tender Offers*, 95 Harv. L. Rev. 1028 (1982). If someone stops you on the street and says, "Say, that's a beautiful watch you're wearing—I'll give you $250 for it," you won't necessarily agree to the sale even if the watch is worth only $100 to you (apart from any sale value it may have). You may want to see whether you can sell it for even more than $250, now that you have an inkling of what its market value may be. Likewise the first tender offer may not be the best. It is true that each shareholder can decide for himself whether he is likely to do better by holding out for a better offer, and if enough decide this way the offer will fail and maybe the offeror, or some other investor, will offer more. But many shareholders are passive investors. They know little about the companies in which they invest or about the market for corporate control. They want to be told whether they should sell their shares now or wait for a better offer to come along. Better yet—for it is difficult to absorb information about a subject you don't know much about—they want management to create a process that will maximize the value of their shares in a takeover situation. That may require the use of some defensive tactics.

One defensive tactic that is permitted and indeed required by federal law is, as we shall see, to have a cooling off period between the announcement and the consummation of a tender offer. Such a period gives the shareholders time to do some shopping around. This is not an unmixed blessing. It reduces the expected gain to the first maker of a tender offer, for now he may have to compete with other offerors and may have to raise his price—a possibility that will reduce the likelihood of a tender offer's being made in the first place. On the other hand, the waiting period creates an opportunity for other investors to make competing offers, and thus encourages an auction of the firm's assets with more than one bidder. Maybe the second effect dominates the first. To take another example, if a corporation offers its key managers "golden para-

chutes" (generous severance pay in the event they lose their jobs because of a takeover), this may make them resist takeovers less; and the benefits to shareholders may exceed the costs of the golden parachutes themselves as well as the effect of the parachutes in making the takeover more costly to the acquiring firm.

Conceivably even the "poison pill" may, if it is not actually lethal, benefit shareholders of the target firm. This wonderfully vivid term refers to a family of shareholder rights agreements which, upon some triggering event such as the acquisition by a tender offeror of a certain percentage of the target corporation's common stock, entitle the remaining shareholders to receive additional shares of common stock (or other securities) at bargain prices. Suppose that the tender offeror makes an offer for 51 percent of the stock of the target firm, knowing that if the offer succeeds he can then force out the minority shareholders by voting his shares for a swap of the target's assets for cash (a cash merger). Although minority shareholders who are squeezed out in this fashion have a legal right to receive the fair value of their shares, that value may be less than either the tender offer price or the value that their shares would command in the market had there been no tender offer. A poison pill triggered by the acquisition of a majority stock interest gives the remaining shareholders more shares. This both improves their position if the tender offer succeeds and makes all shareholders less frantic to tender. Without the poison pill, shareholders will compete to tender their shares because if they do not they may miss out on an opportunity to sell their shares at a premium price and thus to escape the fate of the minority shareholder. But at the same time, by making a tender offer less certain to succeed and more costly to the offeror, the poison pill may reduce the number of tender offers and the price of each offer, thus hurting all shareholders ex ante.

The tradeoffs obviously are complex, so it is no surprise to find that the evidence on whether particular defensive tactics enhance or reduce shareholder welfare is mixed.

See Jensen & Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. Financial Econ. 5, 29-40 (1983). An intriguing recent finding is that targets that resist tender offers yet are later acquired do better, at least in the short run, in maximizing shareholder wealth than targets that do not resist. The qualification is vital; if, as seems likely, defensive tactics reduce the number of tender offers, then shareholders may lose in the long run. Moreover, the study finds that if the target resists so stubbornly that it is not acquired later, its shareholders are made unequivocally worse off. See Jarrell, *The Wealth Effects of Litigation by Targets: Do Interests Diverge in a Merge?*, 28 J. Law & Econ. 151 (1985). But maybe, even with the risk that resistance will be too successful or that defensive tactics may eventually weaken the market for corporate control and hurt all shareholders, some resistance is the optimal strategy for managements perfectly loyal to their shareholders to follow. If so, the adoption of some defensive measures, perhaps even some poison pills, may be in the interest of all the corporation's shareholders, though we are not aware of any rigorous study which finds that poison pills help shareholders.

Personally we are rather skeptical about the arguments for defensive measures. They strike us as giving too little weight to the effect of "defensive" measures in rendering shareholders defenseless against their own managements. (The shareholders of CTS were not asked to approve the poison pill.) We are especially skeptical about the arguments used to defend poison pills. If the present case is representative, the poison pill seems (as we shall see) more a reflex device of a management determined to hold on to power at all costs than a considered measure for maximizing shareholder wealth. Unlike a fair price amendment, which requires the tender offeror to pay the same price to the nontendering as to the tendering shareholders in order to head off a stampede to tender that may reduce the price of the tender offer, the poison pill can (in this case did) substantially dilute the tender offeror's shares, thereby defeating the object of the offer, which is to take

over the company in the hope of squeezing more profit out of its assets. Depending on its terms the poison pill may also make each shareholder think himself better off not tendering, hoping instead to get the goodies that nontendering shareholders receive by virtue of the poison pill. But of course if no one tenders, no tender offer can succeed.

So we have grave doubts about poison pills. But our personal views on a matter committed to the authority of the states are not terribly important; and given the complexity of the issue it is understandable why state courts would hesitate to condemn all defensive measures (even all poison pills) as breaches of fiduciary duty, on the basis of the present incomplete evidence of the actual effects of these measures.

Indeed, the Delaware courts have been quite emphatic that defensive measures in general and poison pills in particular are within the power of the board of directors of a target corporation. E.g., *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 180 (Del. 1986). But at the same time these courts have insisted that the measures be plausibly related to the goal of stockholder wealth maximization. See *id.* ("when a board implements anti-takeover measures, . . . [the] potential for conflict [of interest] places upon the directors the burden of proving that they had reasonable grounds for believing there was a danger to corporate policy and effectiveness, a burden satisfied by a showing of good faith and reasonable investigation"); *Moran v. Household Int'l, Inc.*, 500 A.2d 1346, 1356 (Del. 1985) ("when the business judgment rule applies to adoption of a defensive mechanism, the initial burden [of proving that the directors acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company] will lie with the directors"); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985) ("Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders, there is an enhanced duty which calls

for judicial examination at the threshold before the protections of the business judgment rule may be conferred"). The shifting of burdens adopted in these decisions was anticipated by Judge Cudahy's dissenting opinion in *Panter v. Marshall Field & Co.*, 646 F.2d 271, 299-304 (7th Cir. 1981). See also *Hanson Trust PLC v. ML SCM Acquisition Inc.*, 781 F.2d 264, 273 (2d Cir. 1986) (dictum).

Thus the Delaware courts have not, as CTS argues, written targets' management a blank check endorsed with "business judgment rule." This rule expresses a sensible policy of judicial noninterference with business decisions made in circumstances free from serious conflicts of interest between management, which makes the decisions, and the corporation's shareholders. Not only do businessmen know more about business than judges do, but competition in the product and labor markets and in the market for corporate control provides sufficient punishment for businessmen who commit more than their share of business mistakes. When however there is a serious conflict of interest, and in particular when management is making decisions that may thwart the operation of the market in corporate control, the judicial role (under Delaware law, and we assume Indiana law as well) is less deferential. When managers are busy erecting obstacles to the taking over of the corporation by an investor who is likely to fire them if the takeover attempt succeeds, they have a clear conflict of interest, and it is not cured by vesting the power of decision in a board of directors in which insiders are a minority (five of CTS's eight directors are outsiders). No one likes to be fired, whether he is just a director or also an officer. The so-called outsiders moreover are often friends of the insiders. And since they spend only part of their time on the affairs of the corporation, their knowledge of those affairs is much less than that of the insiders, to whom they are likely therefore to defer.

These problems have seemed serious enough to warrant a more searching judicial review of corporate decisions concerning defensive measures to takeovers than of deci-

sions concerning ordinary business decisions. Such review is not without its costs. It makes directors overcautious, makes people reluctant to serve as directors, drives up directors' fees and officers' and directors' liability insurance rates, and leads boards of directors to adopt ponderous, court-like procedures. But the price is one the courts have been willing to pay.

From these general reflections we turn at last to the particulars of this case. Since the present management of CTS took over the company in 1981, a year after Dynamics first became a major shareholder, CTS's rate of return has declined substantially, in part because of a series of acquisitions to which Dynamics objected and which indeed turned out to be flops. Dynamics therefore coupled its March 10 announcement of the tender offer with a declaration that it would field a slate of candidates for the board of directors election scheduled for April 24 (since postponed). On the very same day (March 10, which was also the day this lawsuit was filed) CTS's management announced its opposition to Dynamics' actions—without having studied their business and financial implications or even having consulted CTS's outside directors. The next day CTS retained as its investment advisor Smith Barney under a contract whereby the advisor would receive a bonus if Dynamics lost the proxy fight. The following day the board met to discuss the matter. Without consulting the board, CTS's chairman wrote the shareholders the next day urging them not to vote for Dynamics' slate. On March 22 Smith Barney presented its poison pill proposal to the board, with an accompanying "fairness opinion" in which it opined that Dynamics' tender offer was unfair but did not opine on whether the $43 price in the offer was fair or unfair. The board did not discuss price either, but did at that very meeting unanimously adopt the poison pill.

The tender offer was not evaluated in a cool, dispassionate, and thorough fashion. We do not mean to suggest that the board was obliged to accord due process to Dynamics; we have no desire to judicialize board of direc-

tors meetings. But it is apparent that the insiders on the board, in particular the chairman, decided from the start to block the tender offer, before its ramifications for shareholder welfare were considered; judgment first, trial later, as the Queen of Hearts said in *Alice in Wonderland*. Smith Barney held itself out as a blocker, and would have lost its $75,000 bonus if it had advised the board that the tender offer was fair and if the end result of this advice had been Dynamics' wresting control of the board from the existing directors. How the fairness of the tender offer could be determined without any consideration of the fairness of the offer price is mystifying. CTS argues that not all the shareholders could get the tender offer price, because Dynamics was seeking tenders of only 17.9 percent of the shares. This is doubly misleading. Every fifth shareholder (.179 divided by .904—the other 9.6 percent of the shares being owned by Dynamics already—is .198) would get that price. More important, all the shareholders benefited ex ante. Upon announcement of the tender offer the price of CTS stock rose from below $36 to above $40 (a much bigger percentage leap than the NYSE Composite, S&P 500, or Dow Jones indexes took that day). Those shareholders who did not expect to be in the lucky one-fifth to sell to Dynamics at $43 could sell the day the offer was announced for $40. (Of course some stockholders would not have known about the movement in the price and some who did know would adhere to a buy-and-hold strategy, and so not sell.) It is worth noting that the price of CTS shares dropped substantially the day after the poison pill was announced, and rose again when the district judge's order invalidating the poison pill was released.

CTS argues that it did not need to investigate the tender offer in order to know it was bad, for there was a long history of bad blood between it and Dynamics. Dynamics had been a very restive, unhappy shareholder. There had been litigation between the companies. CTS's management had formed the judgment that the companies had incompatible philosophies, with CTS focusing on the

long term and hence making substantial capital investments and Dynamics going for the quick buck. It *knew* a takeover of CTS by Dynamics would be bad. But given CTS's disappointing performance in recent years and the fact that Dynamics seemed to have been vindicated in its opposition to CTS's acquisitions by CTS's having written off the largest one as a loss, CTS's management could not be so confident that a takeover by Dynamics would reduce shareholder wealth. The friction between the companies required, if anything, more than the usual amount of care by CTS's board of directors in evaluating the proposal, to make sure that personal feelings would not be allowed to interfere with the board's fiduciary obligations.

All this might be of little moment if the particular poison pill which Smith Barney sold CTS's board were a plausible measure for maximizing shareholder wealth, for as we have said we have no desire to force boards of directors into a judicialized mode of proceeding and we recognize the time pressure under which the board was operating, with the stockholders' meeting scheduled for April 24 and the starting gun for selling stock to Dynamics in response to its tender offer due to go off only 28 days after the announcement of the offer. So let us look at the terms of the poison pill. As soon as one shareholder had 15 percent or more of CTS's stock, all the others would get the right to buy a securities package, consisting of stock and a debenture, for 25 percent of the then market price of the package. The right would thus be triggered if the tender offer went through, and presumably would be exercised since the terms are so advantageous to the shareholder (illustrating our earlier point that poison pills discourage acceptance of tender offers). Assuming that all rights were exercised, the effect of the additional shares that would be issued to the existing shareholders would be to reduce Dynamics' holdings from 27.5 percent of CTS's common stock to 20.7 percent. Not only would this reduce Dynamics' voting power in the election for the board of directors but it would inflict a substantial capital loss on Dynamics. CTS would

be worth no more just because, the "poison pill" having taken effect, the company had more shares outstanding than it did previously. Therefore 20.7 percent of the company would be worth less than the 27.5 percent Dynamics thought it was getting: $24 million less, assuming a $40 price for CTS shares.

In addition, the total amount of debentures to be issued to the shareholders as part of the poison pill would burden CTS with a new, long-term fixed debt of $80 million at a high interest rate (13 percent), further reducing the value of Dynamics' holdings. This large debt, for which CTS would not receive commensurate value in exchange, would reduce CTS's net profits. It could, indeed, imperil its financial health very seriously; for the taking on of such a large debt would entitle some existing creditors of CTS to treat CTS as having thereby defaulted on their loans to it, and these creditors would therefore be entitled to call the loans—and the whole house of cards might collapse. At the very least, the new debt would increase the volatility of CTS's earnings by increasing the fraction of fixed costs in the company's financial structure. This in turn would reduce the value of the stock quite apart from the effect of lower earnings, simply because most investors are risk averse. See, e.g., Lorie & Hamilton, The Stock Market: Theories and Evidence, chs. 11-12 (1973).

We do not want to paint too bleak a picture. Unless the debentures so weighted down CTS with debt that they forced the company into bankruptcy, the shareholders—other than Dynamics, of course—would be getting something of value out of the transaction: the debentures. Their investment in CTS would be converted from an all-equity investment to a package consisting of a riskier equity investment and a debt investment. Indeed, putting aside the effect on Dynamics, the immediate effect of issuing the debentures would just be to raise CTS's debt-equity ratio; and if the ratio was too low before, the shareholders might be made better off. But there is no indication that it was too low before; and if a company's debt-equity ratio is too high, the risk of bankruptcy may become very great.

All this *Sturm und Drang* seems a high price to pay for fending off a change of corporate control that may, for all that appears, benefit the shareholders greatly, though it will be a humiliation to the present officers and directors. It is defended as necessary to protect minority shareholders from a disadvantageous "back-end" transaction. But even after Dynamics obtains 27.5 percent of CTS's stock, it will not be a majority shareholder, and will therefore not be able to squeeze out the remaining shareholders. To be able to do that it will have to buy up another 22.5-plus percent of the shares. CTS's poison pill is thus to be administered prematurely. If the rationale is to protect minority shareholders, it should be triggered by a transaction that creates a majority shareholder or that attempts to squeeze out the minority shareholders, and it should give the minority the same price per share as the majority—not a higher price calculated to kill off the tender, indeed to kill off any tender. CTS's shareholder rights agreement is triggered much earlier, and at a higher price. It effectively precludes a hostile takeover, and thus allows management to take the shareholders hostage. To buy CTS, you must buy out its management.

CTS argues that once Dynamics controls the board of directors and hence the proxy machinery, it will be able to gull the remaining shareholders into selling their shares to it for too low a price. Setting aside the legal remedies against abuse of the proxy machinery, CTS's argument if correct underscores the importance of not impeding tender offers too much, since the premise of the argument is that management cannot be trusted to protect the interests of the shareholders.

We conclude that the poison pill was properly enjoined, and move on to the cluster of issues concerning the distinct takeover obstacle erected by the Indiana control-share acquisition statute, which if valid would thwart Dynamics' tender offer. The Attorney General of Indiana argues that the district judge violated 28 U.S.C. § 2403(b), which provides that in a federal court action in which the

constitutionality of a state statute "affecting the public interest is drawn in question, the court shall certify such fact to the attorney general of the State, and shall permit the State to intervene for presentation of evidence, if evidence is otherwise admissible in the case, and for argument on the question of constitutionality." On April 9 the district judge, who had not yet certified to the state's attorney general that the constitutionality of the Indiana takeover statute was being challenged, held that the statute violated the supremacy clause, because in conflict with the Williams Act. There is a question whether section 2403(b) is meant to apply to cases where the only constitutional challenge is under the supremacy clause, that is, where the state statute is contended to be in conflict with a federal statute. The argument against requiring certification in such a case is that preemption may leave the state statute in force in most of its domain, as in our recent decision in *National Metalcrafters v. McNeil*, 784 F.2d 817, 828-29 (7th Cir. 1986). Whatever the actual force of the argument, the State of Indiana appears to concede the point, for it makes no complaint about the fact that the challenge based on the supremacy clause was not certified to it. On April 16, however, the district judge issued another order, this one holding that the takeover statute also violated the commerce clause; there is no dispute that certification is required in such a case. She did certify—but on April 16, and with oral argument in this court scheduled for April 23 we gave the attorney general only till April 19 to file a brief in this court. He argues that this was not enough time and that at a minimum the April 16 order should be vacated.

Section 2403(b) does not say when the certification must be issued. The suit was not filed till March 10, the constitutional issues did not surface till the complaint was amended on March 31, and ordinarily a delay of less than three weeks in certifying the existence of a constitutional challenge would not be undue. But this was not an ordinary case; and to issue the certification simultaneously with the decision does not comport with the spirit of a statute designed to give the attorney general a fair op-

portunity to argue and if necessary present evidence (only argument is at issue here) to save a state statute. Argument after decision—argument that asks the district court to reconsider its decision or us to reverse it—is an inferior substitute for argument before the district court's decision, which is what the statute obviously envisages though it does not require it in so many words.

Some cases, illustrated by *Bridges v. Phillips Petroleum Co.*, 733 F.2d 1153, 1156 n. 7 (5th Cir. 1984) (per curiam), seem to regard belated certification (e.g., at the appellate level) as adequate compliance nonetheless. A closely related line of cases in the Second Circuit deems it adequate compliance to allow the state to file a brief on appeal without worrying about any formalities of certification. See, e.g., *Doyle v. Suffolk County*, 786 F.2d 523, 526 (2d Cir. 1986). Still other cases, illustrated by *Merrill v. Town of Addison*, 763 F.2d 80, 82-83 (2d Cir. 1985), and by our own decision in *Kealey Pharmacy & Home Care Services, Inc. v. Walgreen Co.*, 761 F.2d 345, 350 n. 8 (7th Cir. 1985), emphasize that failure to comply with section 2403(b) does not deprive the district court of jurisdiction, so that the district court's decision need not be vacated just because certification was belated. In none of the cases we have found, however, did the appellate court hold the challenged state statute unconstitutional, so the issue of the district court's failure to comply with section 2403(b) was not momentous.

In any event section 2403(b) does not prescribe a sanction for its violation; that is left to the courts. And in this case it seems to us the proper sanction (assuming the statute really was violated) is no sanction. The violation was inadvertent, reflecting the very rapid course of the litigation in the district court. The prejudice to the state seems to be nil, for it has yet even to suggest what arguments it might make that counsel for CTS has not made, and it does not want to present any evidence. And the state's apparent lack of interest in challenging the district judge's conclusion that the statute violates the supremacy clause is inconsistent with its passionate interest in challenging her conclusion that the statute also

violates the commerce clause. As we said earlier, a finding of preemption may merely curtail the application of the statute—but not in this case. The district judge held that the only provision of the statute that is in issue is invalid in its entirety under the supremacy clause. This consequence the state contemplates with apparent equanimity; why should it insist on timely certification of a challenge that has the same effect—namely, lethal?

Two other threshold challenges to the district court's constitutional rulings need not detain us for long. The state argues that venue was improper in the Northern District of Illinois; the case should have been brought in Indiana. But objections to venue can be waived, and were waived here by CTS when it failed to follow up its initial objection to laying venue in Illinois. CTS argues that the district court should have abstained in favor of the state courts of Indiana, which might have given a saving construction to the Indiana statute. See *Railroad Comm'n v. Pullman Co.*, 312 U.S. 496 (1941); *Waldron v. McAtee*, 723 F.2d 1348 (7th Cir. 1983). Lack of time is one objection to this course, but the decisive objection is that although there is an issue of state law in this case that affects the constitutional question—whether the Indiana statute is limited to cases where the target corporation is incorporated in Indiana—we have resolved that issue in favor of the state, for we agree that the statute is so limited.

We come then to the merits of the constitutional issues. The issue under the supremacy clause is, as we have said, whether Indiana's control-share acquisition statute is preempted by the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f). The Indiana statute allows a corporation that has more than 100 shareholders and is incorporated in Indiana, and that has its principal place of business, principal office, or substantial assets there, and ten percent of whose shareholders, or 10,000 of whose shareholders, or owners of ten percent of whose shares, reside there, to elect to be covered by the "control share acquisition" provisions of the act; CTS elected. A control share ac-

quisition is defined as an acquisition that along with any previous acquisitions gives the acquirer at least 20 percent of the voting stock of the covered firm. If the acquirer files a statement containing specified information about his intentions and financial capacity (similar to the information required by the Williams Act), management has 50 days within which to hold a special shareholders' meeting to consider whether the acquirer shall have voting rights. A decision in favor of awarding voting rights requires a majority both of all shares and of all "disinterested" shares, that is to say, shares of all shareholders except the acquirer and the officers and inside directors of the corporation. Without these two majorities, the acquirer's shares remain nonvoting shares. If the acquirer does not request a special meeting the question of voting rights will be taken up at the next regularly scheduled stockholders' meeting. And if no acquiring-person's statement is filed the corporation can redeem the acquirer's shares "at the fair value thereof pursuant to the procedures adopted by the corporation."

Cleverly drafted though the statute is to skirt judicial holdings that forbid states to delay tender offers beyond the period required by the Williams Act, the cleverness is fairly transparent. The effect of the Indiana statute is both to impose a 50-day delay on tender offers at the option of the target firm and to make it far more difficult for tender offers to succeed even if delay is not an impediment. The offeror dare not accept the tendered shares till the stockholders' meeting is held, since if he loses the vote on voting rights he will end up with nonvoting shares and will not be able to control the corporation—the main purpose of most tender offers. So he must hold the tender offer open for 50 days, rather than the 28 days required (on average) by the SEC's regulations under the Williams Act. See 17 C.F.R. § 240.14e-1(a) (20 business days). And he can have no great confidence in being able to win the vote on voting rights, since he cannot vote his own shares. Neither can the officers and inside directors, but their aggregate shareholdings will often be small. Not filing an

acquiring-person statement is an unattractive option for the tender offeror; it exposes him to a forced redemption of his shares at a price determined under procedures chosen by a hostile management.

In *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), which affirmed a decision by this court, three Supreme Court Justices opined that Illinois' takeover statute violated the supremacy clause, as we had held, see *MITE Corp. v. Dixon*, 633 F.2d 486, 490-99 (7th Cir. 1980). The Illinois statute, so far as relevant here, required an offeror who tendered for more than 5 percent of a corporation's stock to issue a statement of intentions 20 days before the offer itself could be made. This was in addition to the post-offer waiting period required by the Williams Act. The Illinois statute also required the Secretary of State of Illinois to hold a hearing on the substantive fairness of the offer during the initial 20-day period if requested by a majority of the target's outside directors, or by Illinois owners of 10 percent of the target's stock; and empowered him to disallow the offer if he found that it was substantively unfair.

Most courts have agreed that the Williams Act strikes a balance between target management and tender offeror that the states may not upset. See, e.g., *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d 558, 565-66 (6th Cir. 1982); *National City Lines, Inc. v. LLC Corp.*, 687 F.2d 1122, 1128-33 (8th Cir. 1982). Even *Agency Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029, 1035-39 (1st Cir. 1982), while skeptical of the approach, concedes *some* preemptive force to the Williams Act—probably enough to preempt the Indiana statute. See *id.* at 1038-39. And CTS does not ask us to reexamine our analysis in *MITE*.

Ordinarily when Congress passes a statute punishing some supposedly unfair or unjust practice such as monopolization or misrepresentation, the states are free to add on their own penalties. See *id.* at 1037. If, therefore, the Williams Act is, as a critical literature forcefully argues, see, e.g., Fischel, *Efficient Capital Market Theory, the*

Market for Corporate Control, and the Regulation of Cash Tender Offers, 57 Tex. L. Rev. 1 (1978), an anti-takeover statute, expressing a view, however benighted, that hostile takeovers are bad, one would be hard pressed to argue that the Act forbids the states to pass fiercer anti-takeover statutes. See Note, *Securities Law and the Constitution: State Tender Offer Statutes Reconsidered*, 88 Yale L.J. 510, 512-25 (1979). If intent can be inferred from effect, the characterization of the Williams Act as an anti-takeover statute is reinforced. See Jarrell & Bradley, *The Economic Effects of Federal and State Regulations of Cash Tender Offers*, 23 J. Law & Econ. 371 (1980). However, both we and the Supreme Court plurality in *MITE* pointed out that as the bill that ultimately became the Williams Act wended its way through the labyrinthine processes of Congress, support for hostile takeovers emerged and the original thrust of the bill was somewhat blunted. The importance of the tender offer in disciplining corporate management and shifting corporate assets into the hands of those who can manage them best was remarked, and the legislators' concern narrowed down to making sure that shareholders of target corporations would have enough information to make intelligent decisions. The bill that emerged essentially just requires the filing of a public statement of intentions and giving the shareholders enough time to digest the information in the statement as well as such counterinformation as management may care to supply. Although the ultimate balance that was struck may well incline—too far for some tastes—in favor of target management, that is not inconsistent with an inference that Congress would not have wanted the states to tip the balance any further.

Of course it is a big leap from saying that the Williams Act does not itself exhibit much hostility to tender offers to saying that it implicitly forbids states to adopt more hostile regulations, but this leap was taken by the Supreme Court plurality and us in *MITE* and by every court to consider the question since. The reasoning is that Congress in the Williams Act (as in the federal labor laws)

struck a delicate balance between the contending factions in the takeover controversy and wanted its balance to mean something and not be undone by the states. There is some support for this view in the legislative history, notably in the statement in the House Report that "The bill avoids tipping the balance of regulation either in favor of management or in favor of the person making the take-over bid." H.R. Rep. No. 1711, 90th Cong., 2d Sess. 4 (1968). Admittedly, if this sentence is read with emphasis on the first two words, it ceases to express much if any policy with regard to the permissible scope of state regulation. But whatever doubts of the Williams' Act preemptive intent we might entertain as an original matter are stilled by the weight of precedent. See, besides the other cases we have cited, *Schreiber v. Burlington Northern, Inc.*, 105 S. Ct. 2458, 2463 (1985), and *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 29 (1977).

If the general approach is correct, its application to this case is straightforward. The Indiana statute upsets the balance struck by the Williams Act. Whether it does so more than the Illinois statute struck down in *MITE* is hard to say. The statutes are incommensurable. The Illinois statute both imposed delay and put the acquirer at the mercy of the Illinois Secretary of State; the Indiana statute imposes slightly greater delay but puts the acquirer at the tenderer mercies of the "disinterested" shareholders. If we had to guess we would guess that the Indiana statute is less inimical to the tender offer, but that is unimportant. The Indiana statute is a lethal dose; the fact that the Illinois statute may have been two or three lethal doses has no practical significance. Very few tender offers could run the gauntlet that Indiana has set up. In any event, if the Williams Act is to be taken as a congressional determination that a month (roughly) is enough time to force a tender offer to be kept open, 50 days is too much; and 50 days is the minimum under the Indiana act if the target corporation so chooses.

The question of the Indiana act's validity under the commerce clause may seem doubly academic: if the statute

is unenforceable by reason of the supremacy clause, it hardly matters, at least for this case, whether it is also unenforceable by reason of the commerce clause; and the commerce clause provides an independent bar to state action only when Congress has not spoken. The second point will bear elaboration. All that the commerce clause says is that Congress is empowered to regulate interstate and foreign commerce. Art. I, § 8, cl. 3. Although the clause has long been interpreted to authorize the courts to strike down state regulations of interstate commerce that conflict with the clause's presumed purpose of making the nation a common market, provided that Congress has not spoken, see, e.g., *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299, 319 (1852), one might think that once Congress had spoken the "dormant" commerce clause would fall out and the only judicial function would be to enforce the congressional enactment. Congress has spoken to the interstate traffic in corporate control by passing the Williams Act. If the Act is intended to limit state anti-takeover statutes, that is the authoritative expression of congressional desire, and likewise if the Act is not intended to limit them.

But there is a third possibility: that the Act is intended not to affect their legality one way or the other. In *MITE*, and in the cases that follow it, the courts have separated the supremacy and commerce clause issues—have assumed that the commerce clause retains an independent force despite the enactment of the Williams Act. We shall do the same, if only because of lingering doubt that the Act really was intended to limit state anti-takeover statutes; there is no indication that it was intended to insulate such statutes from complaints that they unduly burden interstate commerce.

The commerce clause has been interpreted to limit the power of the states to impose burdens on people living in other states. The limitation is not absolute; for example, a state may apply its health and safety regulations to imported goods even though the cost of compliance will be borne in part by people in other states, the suppliers of the goods. It is all a matter of balancing the benefit

to the state's residents against the burden to out-of-staters. In this case, as in *Edgar v. MITE Corp., supra*, 457 U.S. 640-46, where a majority of the Supreme Court held that Illinois' anti-takeover statute violated the commerce clause, the balance inclines heavily against the out-of-staters; "the burden imposed on [interstate] commerce is clearly excessive in relation to the putative local benefits." *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970); see *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 471 (1981), and with specific reference to state statutes regulating takeovers, *Mesa Petroleum Co. v. Cities Service Co.*, 715 F.2d 1425, 1429-31 (10th Cir. 1983), and cases cited there, and Levmore, *Interstate Exploitation and Judicial Intervention*, 69 Va. L. Rev. 563, 619-24 (1983). We have not been told the geographical distribution of Dynamics' and CTS's shareholders but we know that CTS need have only a small fraction of its shareholders resident in Indiana to take advantage of the Indiana statute and we can assume that the vast majority of both its shareholders and Dynamics' shareholders are nonresidents. The statute gravely impairs Dynamics' ability to do business with any of CTS's shareholders. Indiana has no interest in protecting residents of Connecticut from being stampeded to tender their shares to Dynamics at $43. See *Edgar v. MITE Corp., supra*, 457 U.S. at 642-43. Unlike a state's blue sky law the Indiana statute is calculated to impede transactions between residents of other states. For the sake of trivial or even negative benefits to its residents Indiana is depriving nonresidents of the valued opportunity to accept tender offers from other nonresidents.

Whether an appreciable number of Indiana shareholders or other Indianans will benefit at all from the statute may be doubted; the only beneficiaries in this case may be the officers and directors of CTS, some of whom may not even be Indianans. No evidence has been presented that a takeover by Dynamics might reduce the value of CTS or lead to a shift of assets or employment from Indiana—and if it did lead to such a shift, this might further condemn,

rather than save, the statute. The commerce clause does not allow states to prevent corporations from moving assets and employees to other states. But whether or not an anti-takeover statute is vulnerable to challenge under the commerce clause if it impedes mobility of corporate assets, it is highly vulnerable if it impedes the important commerce in corporate control. Even if a corporation's tangible assets are immovable, the efficiency with which they are employed and the proportions in which the earnings they generate are divided between management and shareholders depends on the market for corporate control—an interstate, indeed international, market that the State of Indiana is not authorized to opt out of, as in effect it has done in this statute. See *id.* at 643.

L.P. Acquisition Co. v. Tyson, 772 F.2d 201, 205-07 (6th Cir. 1985), is distinguishable. Because the Williams Act was inapplicable to the tender offer there, the disclosures required by the state statute conferred greater benefits on local residents than the disclosure required by the Indiana statute confers, so the balance described in *Pike v. Bruce Church, Inc.* inclined more in favor of protection of local interests. In *Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906, 909-12 (8th Cir. 1984), the required dislosure was designed to give state residents information particularly pertinent to the impact that the takeover would have in the state itself, and the court was persuaded that the effect in discouraging takeovers through delay would be slight—as it is not here. Indiana has erected a barrier at once formidable and arbitrary to tender offers whose principal effects if they succeed will be felt outside Indiana.

The Indiana statute is not saved by the "internal affairs" doctrine. That principle of conflict of laws is designed to make sure that the law of only one state shall govern the internal affairs of a corporation or other association. See *Edgar v. MITE Corp., supra*, 457 U.S. at 645; Restatement (Second) of Conflict of Laws § 302 (1971). In this case the state is indeed Indiana; but it does not follow that any law which Indiana adopts that affects the internal affairs of Indiana corporations is thereby insulated

from review under the commerce clause. We may assume without having to decide that Indiana has a broad latitude in regulating those affairs, even when the consequence may be to make it harder to take over an Indiana corporation; an example is a law that by requiring cumulative voting for the board of directors makes it difficult to oust the entire existing board at one fell swoop. But in this case the effect on the interstate market in securities and corporate control is direct, intended, and substantial; it is not merely the incidental effect of a general regulation of internal corporate governance. The law in question is an explicit regulation of tender offers; that the mode of regulation involves jiggering with voting rights cannot take it outside the scope of judicial review under the commerce clause. Any other conclusion would invite facile evasions of the clause.

The next issue is whether the judge should have enjoined the tender offer on the ground that if it succeeded, Dynamics and CTS would be in violation of section 8 of the Clayton Act. Section 8 prohibits the director of one company from serving as the director of another if the elimination of competition between the companies, as by a merger between them, would violate any of the antitrust laws. The record of this case contains no persuasive evidence that Dynamics and CTS are in competition, but that hardly matters; the important point is that there is no reason to believe that any director of Dynamics will agree to serve as a director of CTS if by doing so he would violate section 8, which is addressed to the director and not the company. Should it wrest control of the board of CTS from the present management and should the firms be found to be in competition, Dynamics will have no difficulty in finding directors for CTS's board who are not also directors of Dynamics.

The last issue is whether the tender offer should have been enjoined because of a failure to disclose material facts. As the district judge correctly found, most of these facts were not material. One was. The tender-offer materials do not disclose Dynamics' intention to oust the present

management of CTS if the tender offer succeeds and enables Dynamics to elect a new board of directors. The district judge held that this omission was cured by the distribution to all shareholders, two weeks before the end of the tender-offer period, of Dynamics' proxy materials, in which it urges the shareholders to elect Dynamics' slate of directors. CTS argues that this was not good enough, because some shareholders may not have paid attention to the proxy solicitation. But such shareholders might have paid equally little attention to the same disclosure in the tender offer. In truth Dynamics' desire to oust the present board was broadcast loudly and widely.

Even if exclusion from the tender offer could not be cured by inclusion in the proxy materials—an arcane question of federal securities law on which CTS's briefs cast little light—it would not follow that enjoining the tender offer was a proper remedy. The fashioning of remedies is largely within the discretion of the district judge and that discretion was not abused in this case.

AFFIRMED.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

IN THE
UNITED STATES DISTRICT COURT
FOR THE
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

DYNAMICS CORPORATION OF AMERICA

Plaintiff,

v.

CTS CORPORATION, et al.

Defendants.

No. 86 C 1624

MEMORANDUM OPINION AND ORDER

SUSAN GETZENDANNER, District Judge:

This action for declaratory and injunctive relief was originally filed to enjoin alleged violations of Section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a), and

Rule 14(a) promulgated thereunder, for noncompliance with applicable SEC rules and misrepresentations in connection with the sending of proxy solicitations. Plaintiff Dynamics Corporation of America ("DCA") is a New York corporation with its principal place of business in Greenwich, Connecticut. Defendant CTS is an Indiana corporation with its principal place of business in Elkhart, Indiana. This court has jurisdiction over the matter pursuant to Section 27 of the Exchange Act, 15 U.S.C. § 78aa, and venue is proper because the defendants are found and transact business in this district.

DCA is the largest beneficial owner of common stock in CTS, owning

approximately 9.7% of CTS' outstanding common stock. Individual defendants Robert D. Hostetler, Gary B. Erekson, Joseph DiGirolamo, George F. Sommer, Gerald H. Frieling, Jr., Don J. Kacek, Ted Ross, and Richard M. Ringoen are all members of the Board of Directors of CTS. Defendants Hostetler, Erekson, and DiGirolamo are also CTS officers. In the complaint, DCA accuses defendants of engaging in an ongoing plan to entrench themselves as current management through a series of "gun-jumping" proxy solicitations.

The same day it filed this action, DCA publicly announced its intention to make a partial tender offer for 1,000,000 CTS shares, which would give it approximately a 27.7% ownership

position in CTS. DCA has indicated that it intends to use these shares to oust current management and elect its own candidates to CTS' Board of Directors at the Annual Meeting of CTS shareholders, scheduled for April 25, 1986.

DCA's tender offer predictably set off a series of defensive maneuvers by the CTS Board and a consequent expansion of the claims and controversies before this court. The sole issue before the court in this opinion is the constitutionality of the Indiana Control Shares Acquisitions Act, Indiana Code, 23-1-42 et seq., a statute which regulates the voting rights of shares acquired as a result of a tender offer or other share

acquisition which results in an ownership position exceeding 20%. This statute is part of a series of amendments to the Indiana Business Corporation Law which were signed into law on March 4, 1986, and which are to become effective August 1, 1987. IND. CODE §23-1-17-3(a). Section 23-1-17-3(b) of the statute, however, permits those corporations which so elect by resolution of the board of directors to be governed by the statute as of April 1, 1986. IND. CODE §23-1-17-3. On March 27, 1986, the CTS Board of Directors by resolution made the new Act applicable to tender offers for CTS shares as of April 1, 1986.

That same day, and before April 1, 1986, CTS filed a declaratory judgment

action in Indiana state court to have the control share acquisition provisions in IND. CODE §23-1-42 declared valid and enforceable. On March 31, 1986, DCA filed its third amended complaint to add a new Count (Count VIII) directed to the new Act and moved for injunctive relief restraining defendants from attempting to enforce the Act in Indiana state court. Defendants represented at a court hearing on April 2, 1986 before Emergency Judge Milton Shadur that they would not take any action in connection with the state court proceeding pending a ruling by this court on the statute's validity and that therefore there was nothing to enjoin. It became apparent in the course of argument, however, that on

March 31, 1986, CTS issued press releases referring to the Board's adoption of the new statute and the statute's effect on DCA's ability to vote its shares. Because those releases were arguably affecting DCA's ability to make a tender offer, the matter was scheduled for expedited ruling on a declaratory judgment motion. 28 U.S.C. §2201.

The basis of DCA's request is that the Indiana Control Shares Acquisition Act violates the Commerce Clause, Article 1, §8, cl.3, and the Supremacy Clause, Article 6, cl. 2, of the United States Constitution. In particular, DCA argues 1) that the Act directly burdens interstate commerce; 2) that the Act's indirect burden on

interstate commerce outweighs any putative local benefits; and 3) that the Act's timing provisions and procedural hurdles conflict directly with the Williams Act by favoring management and building extended delay into the process of making tender offers. CTS, in response, argues that the Act is a permissible exercise of state legislation to govern the internal affairs of a corporation and the relative voting rights of shareholders in Indiana corporations. In order to understand the nature of these challenges, a full explication of the statute is necessary.

Indiana Control Shares
Acquisition Act

Sections 23-1-42-1 through 23-1-42-11 of the new Indiana Business

Corporation Law govern "Control Share Acquisitions," defined as the acquisition by a single entity of shares which give it more than 20 percent of the voting power with respect to shares of an "issuing public corporation." §23-1-42-1. Shares acquired within a 90 day period are considered to have been acquired in a single transaction. §23-1-42-2(b). The Act defines "issuing public corporation" as a corporation that has:

(1) one hundred (100) or more shareholders;

(2) its principal place of business, its principal office, or substantial assets within Indiana; and

(3) either:
(A) more than ten percent (10%) of its shareholders resident in Indiana;
(B) more than ten percent (10%) of its shares owned by Indiana residents; or

(C) ten thousand (10,000) shareholders resident in Indiana.

IND. CODE §23-1-42-4(a). It is undisputed that CTS is an "issuing public corporation" within the meaning of the statute and that DCA's tender offer is a "control share acquisition" which triggers the Act's provisions.

Under the Act, shares acquired in a control share acquisition have voting rights <u>only</u> to the extent granted by resolution approved by the shareholders of the target corporation. In other words, the Act automatically strips the voting rights from such shares unless and until the shareholders resolve otherwise. In order for a tender offeror to regain

the voting rights, the resolution must be approved by:

> (1) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that voting group, . . . <u>and</u>
>
> (2) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that group, excluding all interested shares.

IND. CODE §23-1-42-9(b) (emphasis added). "Interested shares" are defined as shares the voting of which is controlled by an acquiring person, any officer of the corporation, and any employee of the corporation who is also a director of the corporation. §23-1-42-3.

An acquiror under the statute who seeks to avoid the above consequences

may at its election deliver an "acquiring person statement" to the issuing public corporation setting forth certain specified information. §23-1-42-6. If the acquiring person so requests at the time of delivery and undertakes to pay the corporation's expenses of a special meeting, the directors shall call a special meeting of shareholders for the purpose of considering the voting rights to be accorded the shares. If the offeror "so requests," the meeting "must not be held sooner than 30 days after receipt . . . of the acquiring person statement" and the meeting can in any event be delayed up to 50 days after receipt. Otherwise, the voting rights to be accorded the control shares "shall be presented to the next

special or annual meeting of shareholders." §23-1-42-7(a)-(d).

If an acquiror fails to file an acquiring person statement, or if the shares are subsequently not accorded full voting rights, the corporation may, to the extent authorized by its bylaws or articles of incorporation, redeem the shares at their "fair value." If the shares are accorded full voting rights and the acquiring person has acquired a majority of all voting power, the shares may not be redeemed. Upon voter resolution approving the acquisition, the other shareholders have dissenters' rights which enable them to receive the fair value of their shares. "Fair value" as used in both subsections means "a

value not less than the highest price paid per share by the acquiring person in the control share acquisition." §23-1-42-11-(a)-(c).[1]

Jurisdictional Issues

In its briefs filed before Emergency Judge Shadur opposing DCA's motions to amend its complaint and for preliminary relief regarding the Control Shares Acquisition Act, CTS

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[1]One further ramification of the statute is that, unless the CTS board presently approves DCA's acquisition of shares above 10%, CTS would be unable to engage in any business combination with DCA for a period of five years following DCA's acquisition through its tender. See IND. CODE §23-1-43 §18(a). The parties have not mentioned this provision and the court finds that in any event the validity of this provision is not presently ripe for adjudication.

argued that the anti-injunction act would bar DCA's request for relief; that this court lacks Article III jurisdiction for lack of ripeness; and that abstention under the doctrine of Railroad Commission of Texas v. Pullman Co., 312 U.S. 496 (1942) would be proper. Although Judge Shadur either expressly in open court or by clear implication ruled on these jurisdictional arguments when he granted DCA leave to amend its complaint, he also indicated at the hearing that CTS would be free to renew its arguments to me upon my return. Moreover, he entered no written ruling reflecting those determinations. In order to prevent any confusion on the record, the court

deems it appropriate to address those issues in this opinion.

First is CTS's argument that the anti-injunction act would bar this court from enjoining the pending state court action. 28 U.S.C. §2283. This argument is mooted for the moment at least by CTS's concession before Judge Shadur that it would take no action in the state court proceeding until this court ruled on the constitutionality of the Control Shares Acquisition Act. The anti-injunction act does not prevent this court from issuing a declaratory judgment or order requiring CTS to count at the April 25, 1986 shareholders' meeting shares that DCA had acquired in a "control share acquisition." Since DCA does not

presently seek this court to enjoin the state court lawsuit, the court does not reach the issue and will respect the concurrent jurisdiction of the Indiana state court.

Second is CTS's argument that this court lacks jurisdiction under Article III to enter a judgment at this time that the control share provisions of the Indiana Business Corporation Law are unconstitutional. First, CTS argues that DCA is not injured in fact, and that DCA has not established that injury through evidence. Second, CTS argues that the injury is in any event speculative since DCA has admitted that it would not pursue the tender offer if this court upholds CTS's "poison pill" shareholder rights

plan, the validity of which is to be ruled on next week. Both of these arguments are misguided.

The Seventh Circuit has held that a "threat of enforcement of state law" is justiciable under Article III whenever the threat presents "immediate coercive consequences" or "immediate business costs." Alcan Aluminum, Ltd. v. Department of Revenue, 724 F.2d 1284, 1287 (7th Cir. 1984); Nuclear Engineering Co. v. Scott, 660 F.2d 241, 251-52 (7th Cir. 1981), cert. denied, 455 U.S. 993 (1982). In this case, DCA has shown such "immediate business costs." Under the Williams Act time-frame, DCA has the right to purchase CTS shares tendered

to it on April 10, 1986. CTS, however, has unequivocally indicated that it will invoke state law to prevent those shares from being "voted" at the April 25, 1986 shareholders' meeting. That subsequent rulings of this court might cause DCA to withdraw its offer is beyond the point: CTS's threat of enforcing the Control Shares Act has generated uncertainty for DCA in the midst of a heated contest for corporate control. This uncertainty is not speculative nor anticipatory only, but a present fact.

CTS alternatively argues that this court should not address a constitutional issue until it decides other legal issues that may be dispositive

and may avoid the need for constitutional adjudication. Escambia County v. McMillian, 466 U.S. 48, 51 (1984). This principle of jurisprudence, however, is generally invoked in the situation where a party seeks identical relief under both statutory and constitutional grounds. In the present case, DCA has requested under its state law claim in Count VI that CTS be enjoined from enforcing a shareholders rights' plan which would seriously dilute the value of the corporation should DCA acquire over 15%. Under the constitutional claim at issue here, DCA only requests that it be assured the right to vote the shares at the April 25 meeting. The relief requested under the two counts is entirely distinct. While DCA might

withdraw its tender offer in response to other adverse rulings by this court, DCA is under no obligation to do so, and the issue is therefore not one which would be necessarily mooted by a subsequent adverse determination.

The rule adopted here is admittedly not appropriate for all cases. Congress has implicitly if not expressly determined, however, that delay is often a crucial management weapon in the context of a battle for corporate control. Edgar v. MITE Corp., 457 U.S. 624, 637 (1982). Moreover, the impending date of the shareholders' meeting and the pace of this litigation require this court, as far as is possible, to resolve non-factual matters in advance of any

evidentiary hearings. To delay a ruling in this case would unfairly tip the balance of the parties' contest for control in CTS's favor.

Finally, even were this court inclined to await ruling based on potential mootness concerns, CTS has put the constitutionality of the Act squarely in issue by embracing the Act and publicly announcing that its effect is to strip DCA of voting power acquired along with the shares. CTS's decision to issue this press release reflects its belief that the information is "material" under the test of TSC Industries, Inc. v Northway, Inc., 426 U.S. 438 (1976). Because statutes are presumed constitutional, this

court's decision to enforce or invalidate the Act under the facts in this case is obviously a "material" issue of which the shareholders also have a right to know in advance of deciding whether or not to tender shares and/or proxies. As I noted in an earlier order denying DCA certain temporary relief, the "public interest is served if shareholders know exactly where they stand when deciding whether to tender their shares. . . ." That principle will be best served in this case by a prompt ruling on the merits so as to minimize uncertainty.

CTS has argued that the uncertainty on the market is speculative and that DCA should not be entitled to redress shareholder injuries which it

has not suffered and of which there is no evidence. This argument, reasonable in the abstract, nonetheless misses the point. By informing the public of the Indiana Control Shares Act and its effect on DCA's tender, CTS has injected arguably misleading information into the marketplace which this court has the power, if not the duty, to correct. While DCA has indeed argued that market uncertainty exists without presenting evidence to support that claim, this court has relied chiefly on the harm to DCA in its decision that immediate relief is appropriate. Moreover, the materiality test of Northway is an objective one, and needn't be satisfied in every case by actual evidence of market response. In this case, the court

finds as a matter of law that the constitutionality of the Act is material, given CTS's March 31, 1986 press release, and that DCA needn't prove actual market reliance on the information to obtain relief.[2]

For similar reasons, the court rejects CTS's argument for abstention. To abstain would only delay the

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[2] In its opposition brief filed before Judge Shadur, CTS argued that DCA would suffer no irreparable harm by being forced to await this court's decision on the shareholders' rights plan before receiving a ruling on the Control Act's constitutionality. Because DCA is not presently seeking an injunction, the issue needn't be resolved at this moment. The court notes, however, that CTS's argument on irreparable harm is identical with its argument that no Article III controversy exists, and is therefore unpersuasive in any event.

proceedings and compound the potential for confusion in the market. Moreover, CTS has not made the preliminary showing necessary for this court to decline the exercise of its jurisdiction. The abstention doctrine of Railroad Commission of Texas v. Pullman Co., 312 U.S. 496 (1942) is intended to avoid "needless friction with state policies," id. at 500, and should be invoked only where the state statute is "fairly subject to an interpretation which will render [sic] or substantially modify the federal constitutional question." Harman v. Forssenius, 380 U.S. 528, 534-35 (1965). Abstention is not proper merely to give a state court the opportunity to rule first. Wisconsin v. Constantineau, 400 U.S. 433, 438-39

(1971). In this case, CTS has pointed to no ambiguity in the Indiana Control Shares Act the resolution of which would obviate the need for a constitutional ruling. Instead, CTS has simply suggested that an Indiana court "might" find the provisions of the statute unacceptable under the state or federal constitutions. Such vague suggestions are plainly insufficient to support a request for Pullman abstention.

Section 2403(b) Certification

Title 28, section 2403(b) of the United States Judicial Code provides that in any action in a United States court

> to which a State or any agency, officer, or employee thereof is

> not a party, wherein the constitutionality of any statute of that State affecting the public interest is drawn in question, the court shall certify such fact to the attorney general of the State, and shall permit the State to intervene for presentation of evidence, if evidence is otherwise admissible in the case, and for argument on the question of constitutionality.

28 U.S.C. §2403(b). Like its federal counterpart in §2403(a), the requirement of notice and certification is not discretionary. Merrill v. Town of Addison, 763 F.2d 80, 82 (2d Cir. 1985). The cases are divided whether the obligation to certify rests with the court, id., or with the party mounting the constitutional challenge. Kealey Pharmacy & Home Care Services, Inc. v. Walgreen Co., 761 F.2d 345, 350 n.8 (7th Cir. 1985). The cases are uniform, however, in

holding that a failure to certify does not deprive the dis[t]rict court of jurisdiction. Merrill, 763 F.2d at 83; Kealey Pharmacy, 761 F.2d at 350 n.8.

The potential applicability of §2403(b) to this action was first voiced by CTS's counsel at a hearing before Emergency Judge Shadur on April 3, 1986. DCA claims it notified the Indiana attorney general that same day and supplied the attorney general with courtesy copies of relevant pleadings. The attorney general has not responded in the interim. Although DCA maintains that the question of the constitutionality of the Act does not affect the public interest because this case involves only private

parties. The court agrees but only in part. While the Indiana Control Shares Acquisitions Act may affect the public interest for purposes of §2403(b), its impact on the present situation is unique. Therefore, so long as the court confines its discussion to the application of the statute to the facts, and not the validity of the statute itself, the public interest concerns of §2403(b) are not implicated.

That the Indiana attorney general might have intervened earlier does not change this result. DCA has adequately demonstrated that a significant threat to its Williams Act rights exists so as to justify immediate relief from the statute. This harm is

immediate and ongoing, and the effects of applying the statute to this transaction are undisputed. Although DCA has denominated both its Commerce Clause and Supremacy Clause challenges as "facial" challenges to the statute's validity, the applicable cases have persuaded me that the statute's application to DCA under the present circumstances would be unconstitutional under the Supremacy Clause, even if the statute could otherwise be upheld. The court will confine its discussion to the Williams Act issues, since the Commerce Clause challenges, if reached, would have ramifications beyond the present case, and would therefore not be fairly resolved in the state's absence.

Supremacy Clause

Article VI, cl.2, of the United States Constitution provides that "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof, . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the contrary notwithstanding." The issue before this court is whether the Indiana Control Share Acquisitions Act as applied in this case frustrates the congressional objectives of the Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§78m(d)-(e); 78m(d)-(f), [sic] so as to fall within the prohibitions of the Supremacy Clause.

As explained in Edgar v. MITE Corp., 457 U.S. at 632, and in Piper v. Chris-Craft Industries, Inc., 430 U.S. 1, 22 (1977), the Williams Act was passed in response to the increased use of cash tender offers in corporate acquisitions, and to ensure that such devices would be brought within the reach of the disclosure requirements of the federal securities laws. The Act filled a previous regulatory gap by imposing several requirements. First, the Act requires that offerors must, upon commencement of the offer, file detailed information with the SEC, the public, and the target company. 15 U.S.C. §78n(d)(1). Second, the Act sets forth various timing provisions whereby offerors may close their tenders within 30 days,

subject to certain stockholder rights of withdrawal within the first 7 days of a tender and at any time after 60 days of the offer's commencement if the purchase has not been completed. 15 U.S.C. §78n(d)(5). Third, the Act has some fairness provisions to guarantee that all shares tendered must be purchased for the same price, and that excess shares must be purchased on a pro rata basis. 15 U.S.C. §78n(d)(6)-(7).

The primary purpose behind the Williams Act was to protect investors by ensuring adequate disclosure of information. Piper v. Chris-Craft, 430 U.S. at 35. See also Edgar v. MITE Corp., 457 U.S. 624, 633 (1982). As explained in Great Western United

Corp. v. Kidwell, 577 F.2d 1256, 1276 (5th Cir. 1978), rev'd on other grounds sub nom. Leroy v. Great Western United Corp., 443 U.S. 178 (1979), the function of the Act is "to get information to the investor by allowing both the offeror and the incumbent managers of a target company to present fully their arguments and then to let the investor decide for himself." In other words, the goal is to promote shareholder democracy by ensuring a fully informed investing public in corporate control contests.

According to Justice White's plurality opinion in MITE, an important characteristic of the legislation under the Williams Act was "to avoid favoring either management or the

takeover bidder." 457 U.S. at 633. This policy of "evenhandedness" or "neutrality" was implicit in the evolution of the statute, when Congress replaced "avowedly pro-management" disclosure provisions with more neutral requirements which would avoid giving either side additional advantages vis-a-vis the investor in a corporate takeover contest. Id. at 633-34.

The reasons behind this shift are apparent in the legislative history. First, Congress became convinced "that takeover bids should not be discouraged because they serve a useful purpose in providing a check on entrenched but inefficient management." S.Rep.No. 550, 90th Cong., 1st

Sess., 3 (1967). Congress also did not want to deny shareholders the opportunity to sell their shares for a premium over market which results "from the competitive bidding for a block of stock of a given company." 113 Cong.Rec. 24666 (1967) (remarks of Sen. Javits). The disclosure provisions were therefore intended to strike a balance between the investor, management, and the takeover bidder by ensuring that each side would have an opportunity to express and explain its position but no more. See generally MITE, 457 U.S. at 633-34.

Whether the policy of neutrality behind the Williams Act was but a characteristic of legislation directed toward investor knowledge, or was an

affirmative regulatory goal, is in the abstract debatable. See MITE Corp. v. Dixon, 633 F.2d 486, 495 (7th Cir. 1980), aff'd sub nom. Edgar v. MITE Corp., 457 U.S. 624 (1982). In MITE, only three Justices joined Justice White's holding that the Illinois Business Take-Over Act was unconstitutional under the Supremacy Clause. While four Justices simply didn't reach the issue, Justices Powell and Stevens noted that Congress' decision to follow a policy of neutrality was not necessarily "tantamount to a federal prohibition against state legislation designed to provide special protection for incumbent management." 457 U.S. at 655 (Stevens, J., concurring); see also

457 U.S. at 646-47 (Powell, J., concurring).

Despite the above cautionary signals, the majority of courts since MITE have held that state laws which unfairly advantage incumbent management in the context of a battle for corporate control conflict with the Williams Act and are therefore invalid. See L.P. Acquisition Co. v. Tyson, 772 F.2d 201, 207-09 (6th Cir. 1985); Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906, 912-14 (8th Cir. 1984); National City Lines v. LLC Corp., 687 F.2d 1122 (8th Cir. 1982); Icahn v. Blunt, 612 F. Supp. 1400, 1418-1420 (W.D. Mo. 1985). See also MITE Corp. v. Dixon, 633 F.2d at 495 (noting that in 1980 "most courts" had

found state takeover statutes which provide management with a powerful weapon of delay to disrupt the neutrality indispensable for proper operation of the Williams Act). This court sees no need to second-guess these cases simply because the Supreme Court as a whole did not reach the issue, particularly since CTS's counsel mostly ignores MITE in its brief. The court therefore accepts as given the proposition that state legislation which upsets the neutral balance struck by the Williams Act is invalid under the Supremacy Clause.

Justice White's opinion in MITE, like that of the Seventh Circuit below, identified three provisions of the Illinois Act that conflicted with

the Williams Act: first, the requirement of precommencement disclosure for a tender offer; second, the hearing provisions of the Act; and third, the ability of the Illinois Secretary of State to pass on the substantive fairness of a tender offer. 457 U.S. at 634-640. The Court emphasized that the precommencement notification provisions allowed the target company to disseminate information to its shareholders in advance of the offeror's ability to communicate, thereby distinctly favoring management. 457 U.S. at 635. The Court further concluded that the hearing provisions of the Act frustrated Congress' purpose by introducing extended delay into the tender offer process. Id. at 637. The Court held

that delay alone can seriously impede a tender offer and that delays beyond what the Williams Act provides would unduly favor the target company's management and thereby frustrate many pro-competitive cash tenders. _Id_. at 637-38.

In _Icahn v. Blunt_, 612 F. Supp. 1400 (W.D. Mo. 1985), the plaintiff sought injunctive and declaratory relief against the Missouri Control Share Acquisition Statute, a state law somewhat similar to the Indiana legislation at issue here. Under the Missouri statute, a tender offeror seeking to acquire over 20% of a corporation had to deliver an "acquiring person statement" to the target company, which would then have ten

days to call a special meeting of shareholders. This meeting itself was to be held no sooner than thirty and no later than fifty days from the date the statement was received. The statute then required that a purchaser could not complete the control acquisition until two-thirds of all outstanding shares and two-thirds of all outstanding shares, excluding interested shares, had voted in favor of the proposed acquisition. 612 F. Supp. at 1406-07.

The district court found that the statute conflicted with the Williams Act in at least three ways. First, the court noted that the statute expressly prevented tender offerors from commencing their offers directly

to shareholders until after obtaining the requisite supermajority approval. Second, the court found that the statute's fifty day timing provision prevented offerors from purchasing shares within the deadlines set by the Williams Act. Third, the court noted that the statute implicitly favored management by giving it control over the timing of the meeting and the form of the notice to shareholders; by making exceptions for control share acquisitions which management had approved; and by requiring two-thirds approval of all outstanding shares for control acquisitions, under which system all votes not cast would operate as votes against the potential purchaser. 612 F. Supp. at 1419-20.

Under the Indiana Control Share Act, an offeror who wishes to assure acquisition of voting rights prior to close of the tender must notify the target corporation and request a special shareholders' meeting. The timing of the meeting is left to management's discretion so long as it does not exceed 50 days. Thus, the Act allows incumbent management to delay a tender offer well beyond the 20-day timetable of the Williams Act, since the offeror who does not await such a meeting may acquire no voting rights. Indeed, the statute can be read to prohibit management from acting sooner than 30 days from receipt of the request. See §23-1-42-7(d). Finally, the Act requires that the offeror finance the expenses

of the meeting within ten days from the request.

DCA argues that to coordinate a tender offer with the Indiana Act the offeror must tip its hand by filing an acquiring person statement with the target company at least 10 and possibly as much as 30 days before announcing the tender offer, thus creating the kind of pre-offer notification struck down in MITE. The court does not interpret the statute in this manner. The offensiveness of the provision in MITE was the one-sidedness of the rules regarding precommencement communications to shareholders: only management was allowed to make such communications. In this case, the offeror can avoid any one-sidedness by

announcing its offer and holding it open for a longer period.

CTS argues that the Indiana statute, by putting the vote to "non-interested" shareholders rather than to management, fully comports with the Williams Act's policy of strict neutrality between the incumbent management and the prospective acquiror. However, the Illinois Act struck down in MITE put the decision on fairness in the hands of state officials, not management, yet the Supreme Court found management's ability to capitalize on the process for delaying purposes was itself enough to frustrate Congress' objectives. Under the Indiana statute, incumbent management has control over

the time and execution of the special shareholders' meeting. In MITE, the Supreme Court indicated that state laws which build extended delays into the tender offer process are themselves in conflict with federal law. 457 U.S. at 637-38. Thus, delay alone may conflict with the congressional goals since "the takeover bidder should be free to move forward within the time frame provided by Congress." Id. at 634. In this case, however, the delay is admittedly not indefinite, as was the case in MITE.

CTS' argument is secondly weak in that the Indiana Act does not wholly exclude "interested" parties from voting. The acquiring person must get not only a majority of disinterested

votes, but also a majority of each voting group entitled to vote separately. §23-1-42-9(b). The latter provision makes no exceptions for interested shares, and thus the statute would appear to operate exactly as did the Missouri statute in requiring both a majority of all shares as well as a majority of disinterested shares before allowing a control share acquisition.

Finally, "interested shares" do not exclude all members of the Board of Directors, only those directors who are also officers or employees of the corporation. §23-1-42-3. In this case, DCA apparently desires to sweep out all existing directors, a majority

of whom are outsiders and who therefore would be allowed to vote any shares they own. Thus, there is an apparent potential for interested parties being allowed to vote their shares. The parties have not presented evidence, however, as to whether the outside CTS directors have substantial or any holdings of CTS stock.

CTS also argues that the opinion in Icahn is not controlling because the Missouri statute struck down in that case directly blocked the acquisition of shares, whereas the Indiana Act governs only the acquisition of voting rights. Therefore, CTS argues that the statute no more conflicts with the Williams Act than do state

laws regulating voting rights (such as laws requiring supermajority approval for fundamental corporate changes) which also have a deterrent effect on the desirability of cash tender offers.

This argument, superficially persuasive in certain respects, is nonetheless misleading. Voting rights, after all, are an integral part of the ownership interest purchased along with a stock certificate. By limiting the rights that a tender offeror can purchase in a control acquisition, the Indiana Act deprives the transaction of all value and therefore blocks the transaction in practical terms as much as would a direct prohibition on control acquisition. Moreover, as noted in MITE in

the context of a commerce clause discussion, "[t]ender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company." 457 U.S. at 645. The implications of this statement for Williams Act purposes were expressed in Icahn, where the district court found that taking the decision to buy or sell "out of the shareholder and the purchaser" and placing it "in the hands of management and other stockholders" created a direct conflict with §13 of the Williams Act. 612 F. Supp. at 1420. The Indiana statute is barely distinguishable from the Missouri statute in this regard.

CTS has also suggested that Congress last year rejected the need for federal oversight of internal corporate affairs, and that to interpret the Williams Act as governing the transfers of voting rights would do violence to Congress' intent. In 1984, a bill, H.R. 5693, was introduced in Congress that would have restricted the authority of a corporation's board of directors in adopting defensive tactics in takeover contests. The bill was scheduled for a vote by the House in August of 1984. See Annual Review of Federal Securities Regulation, 40 Bus. Law. 977, 1020 (1985). By letter of September 25, 1984, however, Secretary of the Treasury Donald Regan advised the House that the bill would intrude

unnecessarily into state law, and "constitute an unwarranted step toward imposition of a substantive federal corporation law." 16 Sec.Reg.L.Rep. No. 38 (BNA 1984). In response to the above, the bill was removed from consideration by the House. Annual Review, supra, at 1021.

From this legislative history CTS argues that Congress has implicitly decided not to usurp the states' exclusive role of regulating internal corporate affairs. The court, after careful consideration, disagrees as far as this case is concerned. Aside from the usual difficulties involved in ascertaining legislative intent from non-action, there is a serious difference between federal legislation

which would restrict the defensive tactics of corporate directors in responding to a takeover offer, and federal legislation which restricts the states from using the force of state law to ensure that corporate takeover contests rarely occur except with management's permission. Corporate directors, after all, are subject to fiduciary duties whereby shareholders can challenge their actions as being contrary to the best interests of the corporation: when state law authorizes the defensive maneuver, however, this check on managerial self-interest is absent. Thus, Congress' decision not to interfere in matters of internal corporate governance is fully consistent with a determination that states

should not unduly favor management in legislation concerning corporate acquisitions.

This court ultimately need not decide, however, whether the Indiana legislature's attempt to regulate only voting rights and not share acquisitions themselves might be permissible in other cases, nor whether the 50-day delaying provision is itself enough to find the statute in conflict with the Williams Act. In the present fact situation, application of the Indiana Control Shares Act would not merely delay DCA's attempted offer, but would clearly undo it. DCA made its tender on March 14, 1986, with the intention of closing on April 10, 1986 and being able to vote the shares along with any

received proxies two weeks later at the April 25th annual shareholders' meeting. Under the Act, however, DCA cannot vote any of the shares it acquires pursuant to the tender offer unless and until a majority of the CTS shareholders vote to extend voting rights to those shares. Because CTS only opted into the statute on March 27, 1986, thus preventing DCA from requesting a meeting sooner, DCA will be prevented from voting its shares until after the April 25, 1986 shareholders' meeting, at which point the shares would have lost all value to DCA.

Such a situation wholly frustrates the purpose and objective of Congress in striking a balance between the

investor, management, and the takeover bidder in takeover contest. As expressed in MITE, the Williams Act's principle of neutrality derives from congressional determination that takeover bids frequently advance shareholder welfare. 457 U.S. at 633. Under the Indiana Control Shares Act as applied to this case, however, DCA's contest for control would be over before it had begun. Such a result cannot be squared with Congress' policy. The court therefore finds that the statute is unconstitutional as applied to the facts of this case, and that DCA is entitled to declaratory relief.

Conclusion

Accordingly, DCA's motion for declaratory relief on Count VIII of the third amended complaint is granted: The Indiana Control Shares Acquisition Act may not constitutionally be applied to prevent DCA from voting any shares acquired through its tender offer at the April 25, 1986 shareholders meeting.

It is so ordered.

/s/ Susan Getzendahner
United States District Judge

April 9, 1986

IN THE
UNITED STATES DISTRICT COURT
FOR THE
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

DYNAMICS CORPORATION OF AMERICA

Plaintiff,

v.

CTS CORPORATION, et al.

Defendants.

No. 86 C 1624

MEMORANDUM OPINION AND ORDER

SUSAN GETZENDANNER, District Judge:

The facts underlying this action are fully set forth in this court's memorandum opinion and order of April 9, 1986, and will not be repeated here. On that date, this court held

unconstitutional as applied to this case the Indiana Control Shares Acquisition Act, a state statute which by its terms would have operated to prevent plaintiff Dynamics Corporation of America ("DCA") from voting any of the stock acquired through an ongoing tender offer for the stock of defendant CTS Corporation ("CTS"). Because the Indiana Attorney General had not been properly certified pursuant to 28 U.S.C. §2403(b), this court limited its discussion to the plaintiff's Williams Act and Supremacy Clause challenges to the statute and based its decision on the facts of this case. The Indiana Attorney General was notified of this liquidation and given copies of relevant pleadings on April 3, 1986, but he has not sought

to intervene in this action nor submitted any statement of position.

CTS has now moved to certify the April 9, 1986 opinion for immediate appeal under Fed.R.Civ.P. 54(b). The court agrees that there is no just cause for delay, but is concerned that the Court of Appeals, were it to reverse, would simply remand for resolution of the Commerce Clause issues left unresolved in the court's former opinion. Because a draft on those issues had been previously prepared, but was not issued due to §2403(b) concerns, the court has decided to rule on the alternative grounds despite the state's failure to intervene. In this way, the court intends to provide a record whereby the entire

controversy over the effectiveness of the Act can be definitively resolved on appeal. The court will also certify the appeal to the Indiana Attorney General under §2403(b) so that the state will have an opportunity to intervene before the Seventh Circuit. Cf. Merrill v. Town of Addison, 763 F.2d 80, 83 (2d Cir. 1985) (purposes of §2403(b) certification can be satisfied at appellate level).

Both the mechanics of the Indiana statute and various procedural objections voiced by defendants were thoroughly discussed in this court's previous opinion. Because the present opinion is best understood as an amendment or addition to that earlier

opinion, those discussions will not be repeated again today.

Commerce Clause

The Commerce Clause of the United States Constitution, Art. 1, §8, cl. 3, provides that "Congress shall have power . . .[t]o regulate commerce . . . among the several states." Although the clause by its terms refers to congressional power only, it has been long held that the Clause, even without implementing legislation by Congress, acts as a limitation upon state power. Great Atlantic & Pacific Tea Co. v. Cottrell, 424 U.S. 366, 370-71 (1976); Freeman v. Hewitt, 329 U.S. 249, 252 (1946); Cooley v. Board of Wardens, 53 U.S. (12 How.) 299 (1852). A state statute which inci-

dentally regulates interstate commerce will be upheld "unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970), citing Huron Portland Cement Co. v. Detroit, 362 U.S. 440, 443 (1960). Direct regulation of interstate commerce by the states, however, is prohibited. Pike, 397 U.S. at 142; Shafer v. Farmers Grain Co., 268 U.S. 189, 199 (1925).

In Edgar v. MITE Corp., 457 U.S. 624 (1982), the Supreme Court addressed the constitutionality of the Illinois Business Takeover Act. That Act contained several provisions designed to regulate tender offers for

corporations which met two of the following conditions: the corporation had its principal office in Illinois, was organized under Illinois law, or had at least 10% of its stated capital and paid-in surplus represented in Illinois. 457 U.S. at 627, 642. In such circumstances, the Act required an offeror to notify the Illinois Secretary of State of its intention to make a tender offer 20 days before the offer became effective and prevented the offeror from communicating with shareholders during that time. 457 U.S. at 635. Second, the Act permitted the Illinois Secretary of State to hold a hearing to adjudicate the substantive fairness of the tender offer, and in fact required the Secretary of State to call such a hearing

if requested to do so by persons holding 10% of the outstanding shares. Id. at 627. If the Secretary after hearing determined that the offer was unfair, he could deny registration. Id.

A plurality of the Court struck down the statute as unconstitutional under both prongs of the Commerce Clause analysis.[1] First, the Court

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[1]Justice White delivered the opinion for the Court, in which only the Chief Justice joined. Justice Blackmun joined in the opinion only on Williams Act preemption grounds; whereas Justices Stevens and O'Connor concurred in Justice White's commerce clause analysis. Justice Powell's concurrence was limited to Part V-B of the opinion. 457 U.S. at 646. That part relied on the argument that the statute's indirect burdens on interstate commerce outweighed its local benefits. Justices Marshall, Brennan, and Rehnquist dissented on mootness grounds.

held that the Illinois Act directly regulated and prevented interstate tender offers which in turn would generate interstate transactions. The Court noted that the legislation directly regulated interstate transactions, since tender offers are ordinarily communicated and consummated by means of interstate commerce nationwide, and that the Act could be applied to regulate tender offers and to prevent stock transactions which would take place wholly outside the State of Illinois. 457 U.S. at 641-42.

Second, a majority of the Court held that the burdens imposed by the Act on interstate commerce were excessive in light of the local interests the Act purported to further. 457

U.S. at 640.[2] The Court found that the statute effectively enabled the Illinois Secretary of State to block a nationwide tender offer, thereby removing the incentive that tender offers provide to ensure the efficient performance of incumbent management, and that the asserted local interests--the protection of resident security holders and the regulation of internal corporate affairs--were insufficient to outweigh those burdens given the Act's effects on nonresident shareholders and non-Illinois corporations. Id. at 643-44.

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[2]The majority votes were Justices White, Powell, O'Connor, Stevens, and the Chief Justice. See supra footnote 1.

Two district courts have applied the holding of MITE to find other control shares acquisition acts unconstitutional under the Commerce Clause. In APL Limited Partnership v. Van Dusen, Inc., 622 F.Supp. 1216 (D. Minn. 1985), the district court found the Minnesota Control Share Acquisition Act to pose an unreasonable burden on interstate commerce. That statute regulated tender offers for shares in corporations organized under Minnesota law with either their principal place of business of $1,000,000 in assets within the state. The statute required acquirors to disclose certain information to shareholders of the target corporation and permitted the shareholders to block the acquisition through a stockholders vote. The

court found the putative local benefits insufficient to outweigh the severe effects on nonresident stockholders who might wish to tender their shares for a premium.

In Icahn v. Blunt, 612 F.Supp. 1400 (W.D. Mo. 1985), the court found the Missouri Control Share Acquisition Statute, which like the Minnesota statute gave the shareholders power to block a 20% acquisition, an impermissible attempt to assert extraterritorial jurisdiction over nonresident persons and property. The court stressed that the statute was applicable to foreign corporations, was not limited in effect to in-state shareholders, and was therefore a direct regulation of interstate commerce.

The court also found that the statute was unconstitutional under the balancing test of <u>Pike v. Bruce Church, Inc.</u>, 397 U.S. 137 (1970) since the burden imposed on interstate commerce was excessive in relation to the local interests served.

<u>Whether IND. CODE §23-1-42 directly burdens interstate commerce</u>.

DCA argues that the Indiana Control Shares Acquisition Act directly regulates interstate commerce in the following ways:

(1) it permits target company management to strip the voting rights from shares acquired in out-of-state transactions;

(2) it can be invoked by the management of out-of-state companies;

(3) it permits target company management to effectively block successful interstate tender offers.

CTS, in contrast, argues that the statute does not directly regulate tender offers but merely governs the internal relations between existing shareholders once the shares have been acquired. Therefore, CTS argues that the statute is no different from other voting-rights provisions, such as supermajority requirements or cumulative voting, which govern internal corporate affairs.

There is a superficial persuasiveness to CTS's argument. Unlike the statutes in APL and Icahn, the Indiana Control Shares Acquisition Act does not give shareholders the power to block control acquisitions altogether, but only gives power to block the acquisition of voting rights in connection with those shares. Indeed, the APL court, in holding that the acquisition of shares does not implicate internal corporate matters, expressly distinguished state regulations over the exercise of power resulting from an acquisition. 622 F.Supp. at 1223-24. Therefore, CTS argues that the effect on interstate commerce is incidental at best, and that the statute no more deters purchases of stock in Indiana corporations than do laws requiring supermajority shareholder approvals for fundamental corporate changes.

As I noted in my April 9, 1986 opinion, however, this argument ignores the basic fact that voting rights are an integral part of the ownership interest purchased along with a stock certificate. See Mem. Op. & Order at 23. By limiting the rights that a tender offeror can purchase in a control acquisition, the Indiana statute deters tender offers and thereby burdens interstate commerce as much as if the statute blocked the transaction altogether. The statute does not govern the exercise of control share voting power, but prevents the power from ever be-

coming acquired except upon specified events. Moreover, by providing for automatic redemption privileges when offerors fail to file an acquiring person statement in advance of purchase, the Act further regulates interstate tender offers. Indiana cannot recast regulation of tender offers as internal corporate governance by allowing the transaction to go forward but depriving it of value. In either event, the statute undeniably "regulates" interstate commerce by restricting the sale and purchase of stock in interstate transactions.

Moreover, the Act appears by its express terms not to be limited to Indiana corporations. An "issuing public corporation" need only have

"substantial assets" in Indiana and 10,000 resident Indiana shareholders for the statute to apply. IND. CODE §23-1-42-4(a). While the statute generally defines "corporation" as a "corporation for profit that is not a foreign corporation, incorporated under or subject to provisions of this article," §23-1-20-5, the statute is also intended by its general terms to apply to "all foreign corporations that want to transact business in Indiana" after July 31, 1987. §23-1-17-4. Thus, foreign corporations which have up to 90% of their shares owned by non-Indiana residents or which have up to 90% of their shareholders residing elsewhere would be "under or subject to provisions of this article" for purposes of §23-1-

20-5 so long as they transact business in Indiana. As noted in MITE, the Commerce Clause precludes the application of a state statute to commerce that takes place wholly outside the state's borders. 457 U.S. at 642-43. Because the Indiana Control Shares Acquisition Act can be used to regulate stock transactions between non-Indiana residents and a non-Indiana acquiror, it presents the same constitutional infirmities which caused the Supreme Court to strike down the Illinois Takeover statute in MITE.

The statute's application to non-resident corporations is not without some ambiguity. Until August 1, 1987, the Act does not apply to domestic corporations unless their board of

directors adopts a resolution electing to be governed by the statute. §23-1-17-3(b). Since the statute does not give foreign corporations this option, it is possible, by negative implication, to read the statute as not governing foreign corporations for the time being. While such a reading is unlikely, given the specific definition of "issuing public corporation," the court addresses this possibility.

Assuming, arguendo, that the Act applies only to Indiana corporations up till August 1, 1987, this alone might not save the statute from constitutional infirmity. First, the statutory mandate to regulate out-of-state corporations as of August 1, 1987 is clear; the court seriously

doubts that any postponements of that power can be used to disguise the nature of the legislature's true intent, or to recharacterize the statute's effects. Second, even were the statute limited to Indiana corporations, by operation it directly interferes with transactions between non-resident shareholders in an Indiana corporation and non-Indiana offerors. As noted in APL, "regulation of shareholders -- and those who would become shareholders -- is not the same as regulating the corporation itself." 622 F. Supp. at 1223 (emphasis in original). Because the issue is arguable, because the court has not heard from the Indiana Attorney General, and because MITE's "direct regulation" holding commanded only a plurality of

Supreme Court Justices, the court examines whether the putative local benefits of the statute outweigh its burden on interstate commerce.

Whether the burden of IND. CODE §23-1-42 on Interstate Commerce Outweighs its Local Benefits.

DCA argues that even if the Indiana Control Shares Acquisition Act does not directly burden interstate commerce, its indirect burdens far outweigh any local benefits. The parties agree that the applicable test for determining this question is that set forth in Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970):

> Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be

> upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be prompted as well with a lesser impact on interstate activities.

As emphasized in Edgar v. MITE Corp., 457 U.S. 624 (1982), moreover, the mere articulation of a legitimate local interest cannot alone justify a burden on interstate commerce: rather, the court must question whether the interest will in fact be furthered by the statute. Therefore, the test is more appropriately characterized as weighing local benefits rather than local interests against interstate burdens. See APL, 622 F.Supp. at 1221.

With this teaching in mind, it is necessary to examine the local interests behind the Indiana Control Shares Acquisition Act. This task is rendered somewhat difficult by the fact that there is no legislative history before the court, and the statute nowhere articulates the local interests it purports to serve. CTS chiefly argues that the Act simply regulates the relations between existing shareholders and that the state legislature intended to fulfill its traditional duty of regulating corporations in a manner that promotes fair treatment of all shareholders and shareholder control over fundamental corporate events.

The court agrees that Indiana has a legitimate right to govern the internal affairs of its corporations. In MITE, however, the Supreme Court noted that internal corporate governance was an inadequate justification for burdening interstate commerce when the statute in question applied to nonresident as well as resident corporations. 457 U.S. at 645. Here, the Indiana statute by its terms applies not only to Indiana corporations but to corporations with "substantial assets" in Indiana and for which only 10% of the outstanding shares or 10,000 shares (whichever is smaller) are owned by Indiana residents. The statute is thus clearly overbroad in relation to the putative local interest of internal corporate regulation.

Moreover, the application of the statute to nonresident corporations, as in MITE, makes CTS's "proposed . . . justification somewhat incredible." Id.

Second, it is questionable in any event whether internal corporate governance can be legitimately invoked to justify regulation of stock transactions. As noted in MITE, "[t]ender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company." 457 U.S. at 645. Accord, APL, 622 F.Supp. at 1223 (distinguishing regulation of shareholders from regulating the corporation itself). CTS nonetheless argues that the Indiana Act

avoids this problem by regulating only the acquisition of voting power, and not the acquisition of the shares themselves.

As I noted earlier, the distinction between acquisition of shares and acquisition of votes is deceptive. The value of the shares in control acquisitions is inseparable from their voting power, and Indiana should not be allowed to burden interstate tender offers by vetoing voting power any more than it should be allowed to give shareholders veto power over the acquisition itself. Thus, while a state may legitimately regulate the exercise of corporate power once control shares have been acquired, it may not prevent the acquisition of power through out-

of-state transactions simply because local interests are affected.

CTS places particular reliance on the passage of _APL_ which distinguishes between the acquisition of shares and the exercise of power as a result of that acquisition: "The acquisition of shares does not implicate the internal affairs of the target corporation. The use of that power _once the shares have been acquired_ may well be a proper subject of state regulation, but that is not what the MCSAA regulates." 622 F.Supp. at 1223-24 (emphasis in original). CTS maintains that because the Indiana Act regulates the post-acquisition power of control shares and not their purchase, the

statute falls on the other side of the distinction drawn in APL.

The court disagrees. The passage in APL appears to distinguish between rules which regulate the power majority shareholders enjoy over minority shareholders on the one hand and rules which regulate the transferring of shares and of power on the other. The Indiana Business Corporation Law already contains provisions which impose fiduciary duties on majority or controlling stockholders. Thus, it is difficult to see what rational basis is served by directly regulating the transfer of power. Indeed, the statute does not require shareholder approval for the transfer of voting power from one majority group to

another, §23-1-42-2(e), even though the same fiduciary concerns would presumably be triggered. This too undercuts the purported state interest articulated by CTS.

In sum, the Indiana Act, by stripping away voting power from new control shares until the majority of "disinterested" shareholders subsequently approves, significantly interferes with the interstate market for corporate control and limits the rights which can be transferred in that market. That interference cannot be justified on the grounds of local interests which are not even-handedly served by the statute and which are apparently protected elsewhere under Indiana law.

Although CTS does not advance the argument, there are two other conceivable state interests behind the Control Shares Acquisition Act. First is the state's concern in protecting local shareholders. Some such concern can be evidenced from the Act's requirement that issuing public corporations have specified numbers or percentages of Indiana shareholders in order to fall within the Act's provisions. The statute appears not to be limited in its effects to Indiana shareholders, however, in contrast to the antitakeover statutes which passed constitutional muster in L.P. Acquisition Co. v. Tyson, 772 F.2d 201 (6th Cir. 1985) and Cardiff Acquisitions, Inc. v. Hatch, 751 F.2d 906 (8th Cir. 1984). Because Indiana has "no legi-

timate interest in protecting nonresident shareholders," there is "nothing to be weighed in the balance" to sustain the law as it applies to transactions solely between non-Indiana residents. See MITE, 457 U.S. at 644; APL, 622 F.Supp. at 1222; Icahn, 612 F.Supp. at 1417.

In MITE, Icahn, and APL, the statutes in question applied to corporations even though there were no resident shareholders. CTS might therefore argue that the Indiana Control Shares Act is distinguishable because of the substantial number of Indiana shareholders who must be affected before the statute operates. The problem with this argument is that the statute's 10% or 10,000 floor still

allows for substantial interference in a transaction where up to 90% of the affected shareholders reside outside Indiana. As noted in Pike v. Bruce Church, the extent of a permissible burden on interstate commerce depends not only on the nature of the local interest involved, but on whether that interest "could be protected as well with a lesser impact on interstate activity." 397 U.S. at 142. Because Indiana could achieve its goal of protecting in-state shareholders without regulating transactions solely between non-residents, the Act's effect on interstate commerce exceeds the scope reasonably necessary for protecting Indiana residents.

Even if the Indiana Act were construed to be limited to in-state shareholders, substantial questions would remain whether the benefits to local shareholders actually outweighed the burden on commerce. In MITE, the Supreme Court concluded that the benefit to Illinois shareholders from increased disclosure burdens was "for the most part speculative" where the Act increased the risk that an interstate tender offer would fail due to defensive tactics employed by incumbent management. Id. at 645. In this case, the concern for shareholder welfare presents similar problems, since the Act protects shareholders only at the expense of deterring tender offers. Since other state laws already protect shareholders against

majority shareholder misconduct, and since both state and federal laws leave corporate boards free to take reasonable defensive measures against takeovers when in the best interest of the shareholders, the need for added protection against control acquisitions is indeed somewhat speculative. The court does not rely on this analysis, however, since the Act's extension to nonresident shareholders is clear.

A final state goal possibly served by the Control Shares Acquisition Act would be Indiana's interest in protecting its business climate. CTS does not advance this argument, however, and the court finds the argument weak for the reasons set forth in APL

and Icahn. In those cases, Minnesota and Missouri, respectively, argued that they had a legitimate interest in protecting corporations which do significant business in-state from acquisitions which might disrupt that business. The Courts found such an argument to be based on the unsubstantiated assumption that a person who acquires 20% of a local corporation's voting stock is likely to harm the state's business climate. The Courts further found the arguments weak in that neither state had attempted to restrain incumbent management from taking actions which might adversely affect the state business climate. See APL, 622 F.Supp. at 1223; Icahn, 612 F.Supp. at 1417. Both of those

arguments are fully applicable to the present case.

In sum, then, the court finds that the substantial interference with interstate commerce created by the Indiana Control Shares Acquisition Act outweighs the articulated local benefits so as to create an impermissible indirect burden on interstate commerce.

Conclus on

The court amends its April 9, 1986 opinion to add additional grounds for granting judgment to the plaintiff on Count VIII of its third amended complaint, and, finding no just cause for delay, certifies the judgment for immediate appeal under Fed.R.Civ.P. 54(b). The court also certifies the

appeal under 28 U.S.C. §2403(b) to the Indiana Attorney General for purposes of intervention. Plaintiff DCA, as the party raising the constitutional challenges, is charged with the responsibility of today notifying the appropriate state officials of this court's judgment and the appeal.

It is so ordered.

/s/Susan Getzendanner
United States District Judge

April 16, 1986

JUDGMENT - ORAL ARGUMENT

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
CHICAGO, ILLINOIS 60604

Decided April 23, 1986.

Before

Hon. William J. Bauer, Circuit Judge

Hon. Richard D. Cudahy, Circuit Judge

Hon. Richard A. Posner, Circuit Judge

Nos. 86-1601, 86-1608

DYNAMICS CORPORATION OF AMERICA,)
Plaintiff-Appellee,)
Counterdefendant-Appellee,)
)
v.)
)
CTS CORPORATION,)
Defendant-Appellant,)
Counterplaintiff-Appellant,)
)
STATE OF INDIANA,)
Intervenor-Appellant.*)

*Caption omits individual defendants-appellants and individual counter-defendants-appellees.

Appeals from the United States
District Court for the
Northern District of Illinois,
Eastern Division.

No. 86 C 1624

Susan Getzendanner, Judge

This cause was heard on the record from the United States District Court for the Northern District of Illinois, Eastern Division, and was argued by counsel.

On consideration whereof, IT IS ORDERED AND ADJUDGED by this Court that the judgment of the said District Court in this case appealed from be, and the same is hereby, AFFIRMED, with

costs, in accordance with the opinion of this Court filed this date.

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
CHICAGO, ILLINOIS 60604

Argued April 23, 1986

Unpublished Order Not To Be

Cited Per Circuit Rule 35

Decided April 23, 1986.

Before

Hon. William J. Bauer, Circuit Judge

Hon. Richard D. Cudahy, Circuit Judge

Hon. Richard A. Posner, Circuit Judge

Nos. 86-1601, 86-1608

DYNAMICS CORPORATION OF AMERICA,)
Plaintiff-Appellee,)
Counterdefendant-Appellee,)
)
v.)
)
CTS CORPORATION,)
Defendant-Appellant,)
Counterplaintiff-Appellant.)
)

STATE OF INDIANA,)
Intervenor-Appellant.*)

Appeals from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 86 C 1624

Susan Getzendanner, Judge

ORDER

This is an appeal under 28 U.S.C. § 1291(a)(1) by CTS Corporation and three of its directors, and by the Attorney General of Indiana, from a series of orders by Judge Getzendanner of the Northern District of Illinois granting Dynamics Corporation of America a preliminary injunction against the enforcement of CTS's

* Caption omits individual defendants-appellants and individual counterdefendants-appellees.

shareholders' rights ("poison pill") plan, declaring the Indiana Control Share Acquisitions Act unconstitutional under the supremacy and commerce clauses, and refusing to enjoin Dynamics' tender offer for a potentially controlling interest in CTS. The orders were issued between April 9 and 16. We accelerated the briefing and argument of the appeal because Dynamics must decide by close of business tomorrow (April 24) whether to buy the shares that have been tendered, a decision that may be materially affected by the validity of the shareholders' rights plan and of the Indiana statute.

Having now heard argument and conferred on the appeal, we have

decided that Judge Getzendanner's orders should be, and they hereby are, affirmed. We shall issue an opinion in due course explaining the grounds of our decision.

AFFIRMED.

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

NO. 86-1601

DYNAMICS CORPORATION OF AMERICA, Plaintiff-Appellee,	)
v.	)
CTS CORPORATION, <u>et</u> <u>al</u>., Defendant-Appellants,	)
STATE OF INDIANA, Intervenor-Appellant.	)

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 86 C 1624

The Honorable
Susan Getzendanner, Judge

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that

defendant-appellant CTS Corporation hereby appeals to the Supreme Court of the United States from the judgment of the United States Court of Appeals for the Seventh Circuit entered on April 23, 1986. The appeal is from the judgment holding unconstitutional the Indiana Control Share Acquisition Chapter, IND. CODE § 23-1-42-1, et seq.

This appeal is taken pursuant to 28 U.S.C. § 1254(2).

/s/James A. Strain
of

BARNES & THORNBURG
1313 Merchants Bank Building
Indianapolis, Indiana 46204
Telephone: (317) 638-1313

Attorney for defendant-appellant CTS Corporation

[Filed: July 16, 1986]

PROOF OF SERVICE

I, James A. Strain, a member of the Bar of the Supreme Court of the United States, hereby certify pursuant to Rules 10 and 28 of the Supreme Court of the United States that on this 15th day of July, 1986, I served copies of the foregoing "Notice Of Appeal To The Supreme Court Of The United States" by depositing copies in the United States mail, first-class postage prepaid, addressed to

Lowell Sachnoff, Esq.
Sachnoff, Weaver & Rubenstein, Ltd.
30 South Wacker Drive
Chicago, IL 60606

Thomas A. Withrow
Henderson, Daily, Withrow & DeVoe
One Indiana Square
Indianapolis, IN 46204

Linley E. Pearson
Attorney General of Indiana
Arthur Thaddeus Perry
Deputy Attorney General
Office of the Attorney General
219 State House
Indianapolis, IN 46204

/s/James A. Strain

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

JUDGMENT IN A CIVIL CASE

DYNAMICS CORPORATION OF AMERICA)
)
v.)
)
CTS CORPORATION, et al)

CASE NUMBER: [86-C-1624]

/ / Jury Verdict. This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

/ XX / Decision by Court. This action came to trial or hearing before the Court. The issues have been tried or heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED that judgment on Count VIII is entered in favor of the plaintiff and against the defendants. There being no just reason for delay, the Court certifies the judgment for immediate appeal under Fed.R.Civ. 54(b). Enter judgment.

April 16, 1986
Date

H. STUART CUNNINGHAM
Clerk

/s/Barbara J. Brotherson
(By) Deputy Clerk

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

1. The Commerce Clause, U.S. Const. art. I, §8, cl. 3, provides:

> The Congress shall have power to regulate commerce with foreign nations, and among the several states.

2. The Supremacy Clause, U.S. Const. art. VI, cl. 2, provides:

> This constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States,

> shall be the supreme law of the land; and the judges in every state shall be bound thereby, any thing in the constitution or laws of any state to the contrary notwithstanding.

3. The Williams Act Amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f), as amended, provide:

> (d) <u>Reports by persons acquiring more than five per centum of certain classes of securities</u>
>
> (1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered

pursuant to section 78l of this title, or any equity security of an insurance company which would have been required to be so registered except for the exemption contained in section 78l(g)(2)(G) of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940 [15 U.S.C. 80a-1 et seq.], is directly or indirectly the beneficial owner of more than 5 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security at its principal executive office, by registered or certified mail, send to each exchange where the security is traded, and file with the Commission, a statement containing such of the following information, and

such additional information, as the Commission may by rules and regulations, prescribe as necessary or appropriate in the public interest or for the protection of investors--

(A) the background, and identity, residence, and citizenship of, and the nature of such beneficial ownership by, such person and all other persons by whom or on whose behalf the purchases have been or are to be effected;

(B) the source and amount of the funds or other consideration used or to be used in making the purchases, and if any part of the purchase price is represented or

is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 78c(a)(6) of this title, if the person filing such statement so requests, the name of the bank shall not be made available to the public;

(C) if the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the

securities, any plans or proposals which such persons may have to liquidate such issuer, to sell its assets to or merge it with any other persons, or to make any other major change in its business or corporate structure;

(D) the number of shares of such security which are beneficially owned, and the number of shares concerning which there is a right to acquire, directly or indirectly, by (i) such person, and (ii) by each associate of such person, giving the background, identity, residence, and citizenship of each such associate; and

(E) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer, including but not limited to transfer of any of the securities, joint ventures, loan or option arrangements, puts or calls, guaranties of loans, guaranties against loss or guaranties of profits, division of losses or profits, or the giving or withholding of proxies, naming the persons with whom such contracts, arrangements, or understandings have been entered into, and giving the details thereof.

(2) If any material change occurs in the facts set forth in the state-

ments to the issuer and the exchange, and in the statement filed with the Commission, an amendment shall be transmitted to the issuer and the exchange and shall be filed with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a "person" for the purposes of this subsection.

(4) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

(5) The Commission, by rule or regulation or by order, may permit any person to file in lieu of the statement required by paragraph (1) of this subsection or the rules and regulations thereunder, a notice stating the name of such person, the number of shares of any equity securities subject to paragraph (1) which are owned by him, the date of their

acquisition and such other information as the Commission may specify, if it appears to the Commission that such securities were acquired by such person in the ordinary course of his business and were not acquired for the purpose of and do not have the effect of changing or influencing the control of the issuer nor in connection with or as a participant in any transaction having such purpose or effect.

(6) The provisions of this subsection shall not apply to--

(A) any acquisition or offer to acquire securities made or proposed to be made by means of a registration statement under the

Securities Act of 1933 [15 U.S.C. 77a <u>et</u> <u>seq</u>.];

(B) any acquisition of the beneficial ownership of a security which, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, does not exceed 2 per centum of that class;

(C) any acquisition of an equity security by the issuer of such security;

(D) any acquisition or proposed acquisition of a security which the Commission, by rules or regulations or by order, shall

exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purposes of this subsection.

(e) <u>Purchase of securities by issuer</u>

(1) It shall be unlawful for an issuer which has a class of equity securities registered pursuant to section 78<u>l</u> of this title, or which is a closed-end investment company registered under the Investment Company Act of 1940 [15 U.S.C. 80a-1 <u>et</u> <u>seq</u>.], to purchase any equity security issued by it if such purchase

is in contravention of such rules and regulations as the Commission, in the public interest or for the protection of investors, may adopt (A) to define acts and practices which are fraudulent, deceptive, or manipulative, and (B) to prescribe means reasonably designed to prevent such acts and practices. Such rules and regulations may require such issuer to provide holders of equity securities of such class with such information relating to the reasons for such purchase, the source of funds, the number of shares to be purchased, the price to be paid for such securities, the method of purchase, and such additional information, as the Commission deems necessary or appropriate in the public interest or for the protection of

investors, or which the Commission deems to be material to a determination whether such security should be sold.

(2) For the purpose of this subsection, a purchase by or for the issuer or any person controlling, controlled by, or under common control with the issuer, or a purchase subject to control of the issuer or any such person, shall be deemed to be a purchase by the issuer. The Commission shall have power to make rules and regulations implementing this paragraph in the public interest and for the protection of investors, including exemptive rules and regulations covering situations in which the Commission deems it unnecessary or

inappropriate that a purchase of the type described in this paragraph shall be deemed to be a purchase by the issuer for purposes of some or all of the provisions of paragraph (1) of this subsection.

(3) At the time of filing such statement as the Commission may require by rule pursuant to paragraph (1) of this subsection, the person making the filing shall pay to the Commission a fee of 1/50 of 1 per centum of the value of securities proposed to be purchased. The fee shall be reduced with respect to securities in an amount equal to any fee paid with respect to any securities issued in connection with the proposed transaction under section

77f(b) of this title, or the fee paid under that section shall be reduced in an amount equal to the fee paid to the Commission in connection with such transaction under this paragraph.

15 U.S.C. § 78m(d)-(e).

(d) <u>Tender offer by owner of more than five per centum of class of securities; exceptions</u>

(1) It shall be unlawful for any person, directly or indirectly, by use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, to make a tender offer for, or a request or invitation for tenders of, any

class of any equity security which is registered pursuant to section 78l of this title, or any equity security of an insurance company which would have been required to be so registered except for the exemption contained in section 78l(g)(2)(G) of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940 [15 U.S.C. 80a-1 et seq.], if, after consummation thereof, such person would, directly or indirectly, be the beneficial owner of more than 5 per centum of such class, unless at the time copies of the offer or request or invitation are first published or sent or given to security holders such person has filed with the Commission a statement containing such

of the information specified in section 78m(d) of this title, and such additional information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors. All requests or invitations for tenders or advertisements making a tender offer or requesting or inviting tenders of such a security shall be filed as a part of such statement and shall contain such of the information contained in such statement as the commission may by rules and regulations prescribe. Copies of any additional material soliciting or requesting such tender offers subsequent to the initial solicitation or request shall contain such information as the Commission may

by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors, and shall be filed with the Commission not later than the time copies of such material are first published or sent or given to security holders. Copies of all statements, in the form in which such material is furnished to security holders and the Commission, shall be sent to the issuer not later than the date such material is first published or sent or given to any security holders.

(2) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer,

such syndicate or group shall be deemed a "person" for purposes of this subsection.

(3) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

(4) Any solicitation or recommendation to the holders of such a security to accept or reject a tender offer or request or invitation for tenders shall be made in accordance with such rules and regulations as the

Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(5) Securities deposited pursuant to a tender offer or request or invitation for tenders may be withdrawn by or on behalf of the depositor at any time until the expiration of seven days after the time definitive copies of the offer or request or invitation are first published or sent or given to security holders, and at any time after sixty days from the date of the original tender offer or request or invitation, except as the Commission may otherwise prescribe by rules, regulations, or order as necessary or appropriate in the public

interest or for the protection of investors.

(6) Where any person makes a tender offer, or request or invitation for tenders, for less than all the outstanding equity securities of a class, and where a greater number of securities is deposited pursuant thereto within ten days after copies of the offer or request or invitation are first published or sent or given to security holders than such person is bound or willing to take up and pay for, the securities taken up shall be taken up as nearly as may be pro rata, disregarding fractions, according to the number of securities deposited by each depositor. The provisions of this subsection shall also apply to

securities deposited within ten days after notice of an increase in the consideration offered to security holders, as described in paragraph (7), is first published or sent or given to security holders.

(7) Where any person varies the terms of a tender offer or request or invitation for tenders before the expiration thereof by increasing the consideration offered to holders of such securities, such person shall pay the increased consideration to each security holder whose securities are taken up and paid for pursuant to the tender offer or request or invitation for tenders whether or not such securities have been taken up by such

person before the variation of the tender offer or request or invitation.

(8) The provisions of this subsection shall not apply to any offer for, or request or invitation for tenders of, any security--

(A) if the acquisition of such security, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, would not exceed 2 per centum of that class;

(B) by the issuer of such security; or

(C) which the Commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purposes of this subsection.

(e) Untrue statement of material fact or omission of fact with respect to tender offer

It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light

of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.

(f) Election or designation of majority of directors of issuer by owner of more than five per centum

<u>of class of securities at other than meeting of security holders</u>

If, pursuant to any arrangement or understanding with the person or persons acquiring securities in a transaction subject to subsection (d) of this section or subsection (d) of section 78m of this title, any persons are to be elected or designated as directors of the issuer, otherwise than at a meeting of security holders, and the persons so elected or designated will constitute a majority of the directors of the issuer, then, prior to the time any such person takes office as a director, and in accordance with rules and regulations prescribed by the Commission, the issuer shall file with the Commission,

and transmit to all holders of record of securities of the issuer who would be entitled to vote at a meeting for election of directors, information substantially equivalent to the information which would be required by subsection (a) or (c) of this section to be transmitted if such person or persons were nominees for election as directors at a meeting of such security holders.

4. Chapter 42 (entitled "Control Share Acquisitions") of the Indiana Business Corporation Law, IND. CODE ANN. §§ 23-1-42-1 to -11 (Burns Cum. Supp. 1986), provides:

<u>23-1-42-1</u>. <u>"Control shares" defined</u>. -- As used in this chapter,

"control shares" means shares that, except for this chapter, would have voting power with respect to shares of an issuing public corporation that, when added to all other shares of the issuing public corporation owned by a person or in respect to which that person may exercise or direct the exercise of voting power, would entitle that person, immediately after acquisition of the shares (directly or indirectly, alone or as a part of a group), to exercise or direct the exercise of the voting power of the issuing public corporation in the election of directors within any of the following ranges of voting power:

(1) One-fifth (1/5) or more but less than one-third (1/3) of all voting power.

(2) One-third (1/3) or more but less than a majority of all voting power.

(3) A majority or more of all voting power.

23-1-42-2. "Control share acquisition" defined. -- (a) As used in this chapter, "control share acquisition" means the acquisition (directly or indirectly) by any person of ownership of, or the power to direct the exercise of voting power with respect to, issued and outstanding control shares.

(b) For purposes of this section, shares acquired within ninety (90) days or shares acquired pursuant to a plan to make a control share acquisition are considered to have been acquired in the same acquisition.

(c) For purposes of this section, a person who acquires shares in the ordinary course of business for the benefit of others in good faith and not for the purpose of circumventing this chapter has voting power only of shares in respect of which that person would be able to exercise or direct the exercise of votes without further instruction from others.

(d) The acquisition of any shares of an issuing public corporation does

not constitute a control share acquisition if the acquisition is consummated in any of the following circumstances:

(1) Before January 8, 1986.

(2) Pursuant to a contract existing before January 8, 1986.

(3) Pursuant to the laws of descent and distribution.

(4) Pursuant to the satisfaction of a pledge or other security interest created in good faith and not for the purpose of circumventing this chapter.

(5) Pursuant to a merger or plan of share exchange effected in compliance with IC 23-1-40 if the issuing public corporation is a party to the agreement of merger or plan of share exchange.

(e) The acquisition of shares of an issuing public corporation in good faith and not for the purpose of circumventing this chapter by or from:

(1) Any person whose voting rights had previously been authorized by shareholders in compliance with this chapter; or

(2) Any person whose previous acquisition of shares of an issuing public corporation would

have constituted a control share acquisition but for subsection (d);

does not constitute a control share acquisition, unless the acquisition entitles any person (directly or indirectly, alone or as a part of a group) to exercise or direct the exercise of voting power of the corporation in the election of directors in excess of the range of the voting power otherwise authorized.

<u>23-1-42.3</u>. <u>"Interested shares" defined</u>. -- As used in this chapter, "interested shares" means the shares of an issuing public corporation in respect of which any of the following persons may exercise or direct the exercise of the voting power of the

corporation in the election of directors:

(1) An acquiring person or member of a group with respect to a control share acquisition.

(2) Any officer of the issuing public corporation.

(3) Any employee of the issuing public corporation who is also a director of the corporation.

<u>23-1-42-4</u>. <u>"Issuing public corporation" defined</u>. -- (a) As used in this chapter, "issuing public corporation" means a corporation that has:

(1) One hundred (100) or more shareholders;

(2) Its principal place of business, its principal office, or substantial assets within Indiana; and

(3) Either:

(A) More than ten percent (10%) of its shareholders resident in Indiana;

(B) More than ten percent (10%) of its shares owned by Indiana residents; or

(C) Ten thousand (10,000) shareholders resident in Indiana.

(b) The residence of a shareholder is presumed to be the address appearing in the records of the corporation.

(c) Shares held by banks (except as trustee or guardian), brokers or nominees shall be disregarded for purposes of calculating the percentages or numbers described in this section.

<u>23-1-42-5</u>. <u>Law applicable to control share voting rights</u>. -- Unless the corporation's articles of incorporation or bylaws provide that this

chapter does not apply to control share acquisitions of shares of the corporation before the control share acquisition, control shares of an issuing public corporation acquired in a control share acquisition have only such voting rights as are conferred by section 9 [23-1-42-9] of this chapter.

<u>23-1-42-6</u>. <u>Notice of control share acquisition</u>. -- Any person who proposes to make or has made a control share acquisition may at the person's election deliver an acquiring person statement to the issuing public corporation at the issuing public corporation's principal office. The acquiring person statement must set forth all of the following:

(1) The identity of the acquiring person and each other member of any group of which the person is a part for purposes of determining control shares.

(2) A statement that the acquiring person statement is given pursuant to this chapter.

(3) The number of shares of the issuing public corporation owned (directly or indirectly) by the acquiring person and each other member of the group.

(4) The range of voting power under which the control share acquisition falls or would, if consummated, fall.

(5) If the control share acquisition has not taken place:

(A) A description in reasonable detail of the terms of the proposed control share acquisition; and

(B) Representations of the acquiring person, together with a statement in reasonable detail of the facts upon which they are based, that the proposed control share acquisition, if consummated, will not be contrary to law, and that the acquiring person has the financial capacity to make the proposed control share acquisition.

23-1-42-7. Shareholder meeting to determine control share voting rights. -- (a) If the acquiring person so requests at the time of delivery of an acquiring person statement and gives an undertaking to pay the corporation's expenses of a special meeting, within ten (10) days thereafter, the directors of the issuing public corporation shall call a special meeting of shareholders of the issuing public corporation for the purpose of considering the voting rights to be accorded the shares acquired or to be acquired in the control share acquisition.

(b) Unless the acquiring person agrees in writing to another date, the special meeting of shareholders shall

be held within fifty (50) days after receipt by the issuing public corporation of the request.

(c) If no request is made, the voting rights to be accorded the shares acquired in the control share acquisition shall be presented to the next special or annual meeting of shareholders.

(d) If the acquiring person so requests in writing at the time of delivery of the acquiring person statement, the special meeting must not be held sooner than thirty (30) days after receipt by the issuing public corporation of the acquiring person statement.

23-1-42-8. Notice of shareholder meeting. -- (a) If a special meeting is requested, notice of the special meeting of shareholders shall be given as promptly as reasonably practicable by the issuing public corporation to all shareholders of record as of the record date set for the meeting, whether or not entitled to vote at the meeting.

(b) Notice of the special or annual shareholder meeting at which the voting rights are to be considered must include or be accompanied by both of the following:

(1) A copy of the acquiring person statement delivered to the issuing public corporation pursuant to this chapter.

(2) A statement by the board of directors of the corporation, authorized by its directors, of its position or recommendation, or that it is taking no position or making no recommendation, with respect to the proposed control share acquisition.

23-1-42-9. Resolution granting control share voting rights. -- (a) Control shares acquired in a control share acquisition have the same voting rights as were accorded the shares before the control share acquisition only to the extent granted by resolu-

tion approved by the shareholders of the issuing public corporation.

(b) To be approved under this section, the resolution must be approved by:

(1) Each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that voting group, with the holders of the outstanding shares of a class being entitled to vote as a separate voting group if the proposed control share acquisition would, if fully carried out, result in any of the changes described in IC 23-1-38-4(a); and

(2) Each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that group, excluding all interested shares.

<u>23-1-42-10</u>. <u>Redemption of control shares</u>. -- (a) If authorized in a corporation's articles of incorporation or bylaws before a control share acquisition has occurred, control shares acquired in a control share acquisition with respect to which no acquiring person statement has been filed with the issuing public corporation may, at any time during the period ending sixty (60) days after the last acquisition of control shares by the acquiring person, be subject to redemption by the corporation at the

fair value thereof pursuant to the procedures adopted by the corporation.

(b) Control shares acquired in a control share acquisition are not subject to redemption after an acquiring person statement has been filed unless the shares are not accorded full voting rights by the shareholders as provided in section 9 [23-1-42-9] of this chapter.

<u>23-1-42-11</u>. <u>Rights of dissenting shareholders</u>. -- (a) Unless otherwise provided in a corporation's articles of incorporation or bylaws before a control share acquisition has occurred, in the event control shares acquired in a control share acquisition are accorded full voting rights

and the acquiring person has acquired control shares with a majority or more of all voting power, all shareholders of the issuing public corporation have dissenters' rights as provided in this chapter.

(b) As soon as practicable after such events have occurred, the board of directors shall cause a notice to be sent to all shareholders of the corporation advising them of the facts and that they have dissenters' rights to receive the fair value of their shares pursuant to IC 23-1-44.

(c) As used in this section, "fair value" means a value not less than the highest price paid per share

by the acquiring person in the control share acquisition.

(3) (3)

Nos. 86-71 & 86-97

IN THE

Supreme Court of the United States

OCTOBER TERM 1986

CTS CORPORATION,
Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,
Appellee.

STATE OF INDIANA,
Intervenor-Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,
Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MOTION OF APPELLEE DYNAMICS CORPORATION OF AMERICA TO AFFIRM

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QUESTION PRESENTED

Whether the unanimous decision of the Seventh Circuit Court of Appeals forbidding appellant CTS Corporation ("CTS") from applying the Control Share Chapter of the Indiana Business Corporation Law to the tender offer of appellee Dynamics Corporation of America ("DCA") should be summarily affirmed when:

1. The Chapter allows the management of Indiana corporations to delay tender offers for three weeks beyond the period mandated by the Williams Act and it was impossible for DCA's tender offer to comply with the Chapter even though it satisfied all federal requirements;

2. The Chapter insulates Indiana corporations from the interstate market for corporate control, directly regulates transactions between nonresidents and its burden on interstate commerce far outweighs any local benefits; and

3. *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), is dispositive of this case and has provided clear guidance to lower courts considering similar anti-takeover statutes.

PARTIES TO PROCEEDINGS BELOW

In the Seventh Circuit No. 86-1601, which involved the constitutional questions presented by this appeal, the parties in the Seventh Circuit were: DCA, as plaintiff-appellee; CTS, Robert Hostetler, Gary Erekson and Joseph DiGirolamo (officers and/or directors of CTS) as defendants-appellants; and the State of Indiana ("Indiana") as intervenor-appellant.

Seventh Circuit No. 86-1608 involved the same action in the District Court, was consolidated with No. 86-1601, but did not involve the constitutional questions presented by the present appeal. The parties were: DCA, Andrew Lozyniak, Edward J. Mooney, Henry V. Kensing, Patrick J. Dorme, Frank A. Gunter, Curtis T. Roff, Saul Sperber, Joseph P. Walker and Harold Cohan (officers and/or directors of DCA) as plaintiffs-appellees; and CTS, Robert D. Hostetler, Gary B. Erekson, Joseph DiGirolamo, George F. Sommer, Gerald H. Frieling, Jr., Don J. Kacek, Ted Ross and Richard M. Ringoen (officers and/or directors of CTS) as defendants-appellants.

Rule 28.1 Listing. Appellee DCA has no parent corporation, non-wholly owned subsidiaries, or affiliates.

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ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MOTION OF APPELLEE DYNAMICS CORPORATION OF AMERICA TO AFFIRM

CONSTITUTIONAL PROVISIONS & STATUTES INVOLVED

This case involves the following constitutional provisions and statutes:

1. The Supremacy Clause, U.S. Const. art. VI, cl. 2.

2. The Commerce Clause, U.S. Const. art. I, § 8, cl. 3.

3. The Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(c), 78n(d)-(f).

4. The Control Share Acquisitions Chapter of the Indiana Business Corporation Law, Ind. Code Ann. §§ 23-1-42-1 to -11 (Burns Cum. Supp. 1986).

PRELIMINARY STATEMENT

I. CTS OPTED INTO THE CONTROL SHARE CHAPTER TO DEFEAT DCA'S TENDER OFFER AND PROXY CAMPAIGN

This appeal arises out of an all-out effort by the current management and directors (collectively "management") of appellant CTS Corporation ("CTS") to preserve their control over CTS in the face of a challenge to their hegemony by appellee Dynamics Corporation of America ("DCA"). At issue is the preservation of the interstate market for corporate control from a protectionist piece of state legislation that conflicts directly with the timing requirements and investor protection purpose of the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f). In striking down CTS' application of the Control Share Acquisitions Chapter of the Indiana Business Corporation Law, Ind. Code § 23-1-42-1 *et seq.* ("Control Share Chapter" or "Chapter") to DCA's tender offer, the Seventh Circuit consistently applied this Court's precedents. Its decision should be summarily affirmed, because *Edgar v. MITE Corp.*, 457 U.S. 624 (1982) is dispositive and the unique circumstances of this case make it an inappropriate vehicle for plenary review.

On March 10, 1986, DCA, then CTS' largest shareholder, commenced a tender offer for 1,000,000 additional shares of CTS stock. The offer was designed to expire on April 10, 1986, twenty business days later. DCA also announced a proxy solicitation campaign to elect its slate of nominees to the CTS Board of Directors at the April 25, 1986 Annual Meeting ("Annual Meeting"). Voting the 1,000,000 shares it would acquire in its tender offer was a key part of DCA's election strategy.

CTS vigorously attempted to block DCA's tender offer and proxy solicitation from the date they were announced.[1] CTS has not denied that it rushed to adopt the Control Share Chapter on March 27, 1986 for that purpose.[2] On March 31, 1986, CTS announced its adoption of the Chapter and stated that it intended to use the Chapter to strip the voting rights from the shares DCA acquired through its tender offer. (App. 85) CTS also stated in filings with the District Court that it would not hold a special shareholders meeting on the voting rights issue before the Annual Meeting, thus making it futile for DCA to attempt to satisfy the requirements of the Chapter. (App. 84)

As intended, CTS' actions directly and adversely affected DCA's tender offer and proxy campaign. On the one hand, DCA's tender offer made no economic sense if DCA could not vote at the Annual Meeting the tendered shares—for which DCA had offered a substantial premium—in favor of its slate of directors. On the other hand, CTS' hasty adoption of the

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[1] Among other things CTS (1) invoked the Indiana Business Take-over Offers Act, Ind. Code § 23-2-3.1 *et seq.*, by requesting a

(Footnote continued on following page)

(Footnote continued from preceding page)

hearing before the Indiana Securities Commissioner and filing an action in Indiana state court seeking to halt DCA's tender offer; (2) filed numerous counterclaims seeking to enjoin DCA's tender offer and proxy solicitation on the grounds that, *inter alia*, DCA's disclosures were misleading and seating DCA's nominees on the CTS Board would violate Section 8 of the Clayton Act, 15 U.S.C. § 19; (3) adopted in succession two "poison pill" shareholder rights plans designed to thwart DCA's tender offer and proxy solicitation; and (4) issued false and misleading communications in connection with its adoption of the second poison pill. The District Court, Seventh Circuit and Indiana Securities Commissioner have rejected all of CTS' defensive measures except for the second poison pill, the legality of which is now on appeal before the Seventh Circuit.

[2] The Control Share Chapter is part of the revised Indiana Business Corporation Law, Ind. Code §§ 23-1-17-1 to 23-1-54-2 (Burns Cum. Supp. 1986), and is attached in the Appendix along with other pertinent statutory provisions. Indiana corporations were permitted to adopt the Business Corporation Law after April 1, 1986. § 23-1-17-(b)(2). Corporations adopting the Business Corporation Law may exempt themselves from the Control Share Chapter. § 23-1-42-5. CTS was the first Indiana corporation to adopt the Business Corporation Law and in its haste filed two notices with the Indiana Secretary of State. (App. 86-89)

Chapter after DCA announced its tender offer and CTS' refusal to hold a prompt special shareholders meeting on the voting rights issue made it impossible for DCA's tender offer to satisfy the requirements of the Chapter even though it complied fully with the Williams Act. This dilemma left DCA with no alternative but to halt both its tender offer and proxy campaign until April 23, 1986, when the Seventh Circuit affirmed the District Court's declaratory judgment that CTS could not apply the Chapter to DCA in connection with DCA's tender offer. DCA promptly purchased 1,000,000 of the tendered shares.

II. THE CONTROL SHARE CHAPTER IS A POWERFUL PRO-MANAGEMENT WEAPON DESIGNED TO DEFEAT TENDER OFFERS

A. The Operation of the Chapter

Once a corporation has opted into the Control Share Chapter its management automatically strips the voting rights from the shares ("control shares") acquired by a party whose total holding of common stock will exceed certain ownership thresholds beginning as low as 20%. § 23-1-42-1. Voting rights can be reattached to the control shares *only* on the basis of a convoluted process which is completely controlled by management. Management is solely responsible for preparing, presenting to shareholders and taking a position on a voting rights resolution, § 23-1-42-8, and voting rights can be reattached "only to the extent granted by [this] resolution," § 23-1-42-9(a). If the resolution fails, management can redeem the acquiror's shares in a process and at a valuation wholly under its control. § 23-1-42-10(b).

This process presents the acquiror with a Hobson's choice. If the acquiror files an "acquiring person statement," § 23-1-42-6, majorities of at least two different shareholder groups must approve management's voting rights resolution:

(1) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that voting group . . .; *and*

(2) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that group, excluding all interested shares.

Ind. Code § 23-1-42-9(b) (emphasis added).[3]

Once a party has filed an acquiring person statement, management has fifty days to present its voting rights resolution to the shareholders. § 23-1-42-7(b). Management is not required to hold a special shareholders meeting before the scheduled expiration of a tender offer and the Chapter does not allow a tender offeror to accelerate the meeting. The Chapter only allows the tender offeror to ensure that the special meeting "not be held *sooner* than thirty days" after the acquiring person statement is filed. § 23-1-42-7(d) (emphasis added).

Alternatively, the acquiror may choose not to file an "acquiring person statement," in which case it is faced with the other prong of the Hobson's choice. The acquiror who does not file an acquiring person statement is at the mercy of management, which may redeem its shares "pursuant to procedures adopted by the corporation," § 23-1-42-10(a), and may delay shareholder consideration of a voting rights resolution until the next annual meeting, § 23-1-42-7(c).

The Control Share Chapter comes into play even if the tender offeror, the management of the target company and 90% of the target company's shareholders are nonresidents. § 23-1-

[3] In control share transactions that implicate §23-1-38-4(a) of the Indiana Business Corporation Law, more than two voting groups must approve the voting rights resolution. *See* §23-1-42-9(b)(1). Appellants' self-serving interpretation of §23-1-42-9(b), CTS Br. at 5 n.3, Indiana Br. at 20 n.*, is contrary to its plain language and the interpretations of the District Court, CTS App. 38-39, the Seventh Circuit, Slip. op. at 20, and other courts that have considered similar requirements, *see Fleet Aerospace Corp. v. Holderman,* No. C-2-86-0556 (S.D. Oh. June 11, 1986), Slip. op. at 12, *aff'd* Fed. Sec. L. Rep. (CCH) ¶92,800 (6th Cir. June 25, 1986) (App. 103); *Icahn v. Blunt,* 612 F. Supp. 1400, 1406-1407 (W.D. Mo. 1985).

42-4(b). The Chapter thus permits the out-of-state management of an Indiana corporation to strip the voting rights from shares tendered by out-of-state shareholders to an out-of-state acquiror in response to a nationwide tender offer that complies with federal law. To the extent the Chapter deters tender offers, it chills a myriad of potential securities transactions with and between nonresidents.

The extraterritorial reach of the Control Share Chapter is especially evident in this case. CTS is an Indiana corporation and DCA is a New York corporation headquartered in Connecticut. Both companies are publicly owned and their stock is traded on the New York Stock Exchange. Approximately two-thirds of the CTS shareholders reside outside of Indiana. Transcript of Proceedings, March 28, 1986, pg. 56. (App. 91)

B. The Chapter Falls Most Heavily on Tender Offers

The market for corporate control allows parties who can make more efficient and profitable use of a company's resources to obtain control over the company.[4] The propensity of management to resist value-maximizing corporate control transactions is well-known. *See generally* Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer,* 94 Harv. L. Rev. 1161 (1981). Tender offers are the most common method used by a party to obtain control of a company whose management has not made efficient use of corporate assets, thereby diminishing shareholder wealth. Tender offers are extended directly to the shareholders, allowing acquirors to sidestep entrenched management and take their case for a change in control directly to the shareholders.

It is evident that the Control Share Chapter was designed to be used against tender offers that are opposed by incumbent

[4] This market is extremely large. In 1985 there were 3,001 corporate control transactions of $500,000 or more. 3 *Corporate Control Alert* 1 (April 1986). (App. 143) The total purchase price of these transactions was $179.6 billion. *Id.* at 9. (App. 144)

management. *First,* by stripping away voting rights, the Chapter falls much more harshly on tender offerors, who always buy shares for their voting rights, than upon other acquirors, who typically buy stock for investment purposes. The value of voting rights to tender offerors is reflected in the high premiums they pay to shareholders.[5] *See generally* Jensen & Ruback, *The Market for Corporate Control: The Scientific Evidence,* 11 J. Fin. Econ. 5 (1983) (collecting studies showing that shareholders reap high premiums from changes in corporate control).

Second, by stripping away the voting rights from only the block of shares which puts the holder over an ownership threshold, §§ 23-1-42-2, -9(a), the Control Share Chapter once again most affects tender offerors, who unlike other acquirors invariably purchase substantial blocks of shares.

Third, the delay built into the Chapter is far more prejudicial to tender offerors than to persons who acquire control shares solely for investment purposes. The Chapter allows management to delay a special shareholders meeting on the voting rights issue for fifty days, in practical terms forcing tender offerors to delay completion of tender offers for over three weeks beyond the twenty business day (approximately 28 calendar day) period mandated by regulations under the Williams Act, 17 C.F.R. § 240.14e-1(a). This three week delay gives management ample time to install defensive measures ("poison pills," sale of "crown jewels," "lock-ups," "pac-man" defenses, self-tenders, etc.), to search for a "white knight" acquiror, and to give themselves lucrative severance benefits. *See* Langevoort, *State Tender-Offer Legislation: Interests, Effects and Political Competency,* 62 Cornell L. Rev. 213, 238 (1977) (delay is "the most potent weapon in a tender offer fight").

Fourth, the byzantine pro-management provisions of the Control Share Chapter give hostile management an *additional*

[5] "The most important shareholder right is the right to cast votes, equal to the number of shares he holds, for membership in the corporation's board of directors." R. Posner, *Economic Analysis of Law* 302 (2d. ed. 1977).

powerful weapon to oppose tender offers. Management already can oppose a tender offer on the merits, in communications with shareholders required under the Williams Act, 17 C.F.R. § 240. 14d-9(f), and by resorting to an arsenal of potent legal weapons under federal securities laws.[6] In sharp contrast, management has no comparable regulatory scheme to deploy in conjunction with the Chapter against other types of control share transactions.

Fifth, the application of the Control Share Chapter to tender offers has far-reaching effects on all shareholders, each of whom is a tender offeree. In contrast, other control share transactions typically involve only the acquiror and a transferee.

[6] Entrenched management can also utilize the antitrust laws, the common law and other state and federal causes of action as well as implement defensive measures like poison pill shareholder rights plans that may be authorized under state law. The new Indiana Business Corporations Law expressly authorizes the management of Indiana corporations to adopt defensive measures against corporate takeovers without shareholder approval. Ind. Code §23-1-22-4.

ARGUMENT

III. THE CONTROL SHARE CHAPTER IS PREEMPTED BY THE WILLIAMS ACT

The Control Share Act is preempted because it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in enacting the Williams Act. *Hines v. Davidowitz,* 312 U.S. 52, 67-68 (1941). The Chapter is also preempted in this case because it was impossible for DCA's tender offer to comply with its provisions even though it satisfied all of the requirements of the Williams Act. *See Florida Lime and Avocado Growers, Inc. v. Paul,* 373 U.S. 132, 142-43 (1963).

A. The Williams Act Embodies a Policy of Neutrality Between Tender Offerors and Management

This Court has already exhaustively examined the legislative history of the Williams Act and concluded that Congress "expressly embraced a policy of neutrality" between tender offerors and the management of target companies. *MITE,* 457 U.S. at 633. In enacting the Williams Act:

> . . . Congress intended to strike a balance between the investor, management, and the takeover bidder. The bidder was to furnish the investor and the target company with adequate information but there was no intention to do more than give incumbent management an opportunity to express and explain its position. Once that opportunity was extended, Congress anticipated that the investor, if he so chose, and the takeover bidder should be free to move forward within the time frame provided by Congress.

MITE, 457 U.S. at 634 (citation and quotation omitted); *see also Schreiber v. Burlington Northern, Inc.,* 472 U.S. ____, 105 S. Ct. 2458, 2463, 86 L.Ed. 2d. 1, 8 (1985) ("The expressed legislative intent was to preserve a neutral setting in which the contenders could fully present their arguments."); *Great Western United Corp. v. Kidwell,* 577 F.2d 1256, 1276-1281 (5th Cir.

1978), *rev'd on venue grounds sub. nom. Leroy v. Great Western United Corp.*, 443 U.S. 173 (1979).[7]

This policy of neutrality is "a major aspect of the effort to protect the investor," *MITE*, 457 U.S. at 633, and complements the disclosure requirements and other investor protections of the Williams Act. Congress recognized the salutary effects of tender offers and "expressly disclaimed an intention to provide a weapon for management to discourage takeover bids or prevent large accumulations of stock which would create the potential for such attempts." *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 58 (1979).

B. The Chapter Conflicts Directly With the Williams Act

Like the anti-takeover statute struck down in *MITE*, the chief vice of the Control Share Chapter is the delay it injects in the tender offer process. The Chapter allows management to delay a special shareholders meeting on the voting rights issue for fifty days. The Williams Act permits the tender offeror to close a tender offer after twenty business (28 calendar) days. No rational tender offeror, however, will buy shares until the voting rights issue is settled. The Chapter thus prevents tender offerors from completing timely tender offers that satisfy all the requirements of the Williams Act as surely as a flat prohibition against completing tender offers in less than fifty days.

[7] Contrary to CTS' argument (CTS Br. at 14-16), *Piper v. Chris-Craft Industries*, 430 U.S. 1 (1977), where this Court refused to grant tender offerors an implied cause of action under §14(e) of the Williams Act, is fully consistent with this policy of neutrality. This Court correctly recognized that giving tender offerors an implied cause of action under §14(e) would undermine the policy of neutrality by giving tender offerors a new and powerful weapon that would impermissibly tilt the balance in their favor in contests for corporate control. *See also Schreiber v. Burlington Northern, Inc.*, 472 U.S. ____, 105 S. Ct. 2458, 2464, 86 L.Ed.2d. 1, 10 (1985)(limiting scope of §14(e) to avoid "inject[ing] uncertainty in the tender offer process").

A more direct conflict between federal and state regulatory schemes can hardly be imagined, especially since Congress in drafting the Williams Act recognized that delay deters wealth-maximizing tender offers by giving entrenched management more time to implement defensive measures. Congress thus rejected proposed precommencement notification requirements that would have delayed tender offers for *shorter* periods than under the Control Share Chapter. *See MITE*, 457 U.S. at 635-38.

Less dramatically, but just as effectively, the other burdensome and pro-management requirements of the Control Share Chapter also frustrate the investor protection objective of the Williams Act. By subjecting tender offers to the approval of at least two shareholder groups, the Chapter interferes with the individual shareholder's right to make its own decision whether to tender. *See MITE*, 457 U.S. at 639 ("Congress intended for investors to be free to make their own decisions."); *Fleet Aerospace Corp. v. Holderman*, No. C-2-86-0556, slip op. at 22-23 (S.D. Oh. June 11, 1986), *aff.'d* Fed. Sec. L. Rep. (CCH) ¶ 92,800 (6th Cir. June 25, 1986). (App. 113-14) The shareholder approval process also superimposes a proxy contest on the tender offer. Management can exploit the proxy rules to delay tender offers beyond fifty days,[8] while the high costs of a proxy contest deter tender offers altogether. *Id.* at 21-22. (App. 112-13)

CTS and Indiana argue implausibly that the Congressionally mandated policy of neutrality places no limits on the power of the states to implement restrictive anti-takeover laws that severely disadvantage tender offerors. Their inverted view of federalism, however, was repudiated by *MITE* and totally ignores the clear conflict between the specific timing require-

[8] If management delays a tender offer for only ten additional days, under the Williams Act shareholders obtain withdrawal rights whose exercise will scuttle a tender offer altogether. *See* 15 U.S.C. § 78d(5).

ments under the Williams Act and the lengthy delay built into the Control Share Chapter.[9]

C. The Control Share Chapter Imposes Conflicting Obligations on DCA and Other Tender Offerors

DCA's tender offer could not comply with the Control Share Chapter even though it satisfied all the Williams Act requirements. Where it is impossible for a party to comply with both state and federal laws, the state law is preempted in favor of the federal requirements. *Florida Lime and Avocado Growers, Inc. v. Paul,* 373 U.S. 132, 142-43 (1963).

DCA's tender offer was scheduled to close on April 10, 1986, twenty business days after it was announced. DCA intended to vote the shares it acquired for its slate of director nominees at the Annual Meeting. As both the District Court and Seventh Circuit found, DCA's tender offer complied with all the requirements of the Williams Act.

It was not until *after* DCA announced its tender offer that CTS rushed to embrace the Control Share Chapter. It chose not to hold a special shareholders meeting on the voting rights issue until after both the date DCA's tender offer expired and the Annual Meeting. CTS apparently intended to wait a full fifty days to present its voting rights resolution. Had DCA waited the fifty days, it would have been forced to extend an otherwise lawful and heavily oversubscribed tender offer and been unable to vote any of the tendered shares on behalf of its director slate at the Annual Meeting.

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[9] Section 28(a) of the Securities Exchange Act ("Exchange Act"), 15 U.S.C. § 78bb(a), which simply restates the Supremacy Clause by stating that state laws not in conflict with the Exchange Act are not preempted, is not to the contrary. Section 28 was enacted to preserve state blue sky laws and was passed decades before tender offers became common, the Williams Act had been passed, and states had begun to insulate local companies against takeovers. *See generally Great Western United Corp. v. Kidwell, supra.,* 577 F.2d at 1271, 1275-76.

Indiana's argument that future tender offerors can avoid such problems by substantially lengthening or heavily conditioning their tender offers (Ind. Br. at 40-43) is irrelevant.[10] This appeal concerns only CTS' application of the Control Share Chapter to DCA's tender offer, which made it impossible for the tender offer to comply with the Chapter even though it met all federal requirements.

The Control Share Chapter presents *all* tender offerors with another impossible dilemma. The Williams Act regulations require a tender offeror to make its offer effective within five days of publicly announcing the material terms. 17 C.F.R. § 240.14d-2(b). An acquiring person statement under the Control Share Chapter undoubtedly constitutes a public announcement of a tender offer. *See* 17 C.F.R. § 240.14d-2(b)-(c). On the one hand, the tender offeror can go ahead with a tender offer even though five days is insufficient time to hold a special shareholders meeting on the voting rights issue. A tender offer, however, makes no economic sense if the tendered shares will be stripped of their voting rights. And to protect their own voting rights against dilution, shareholders have every incentive *not* to grant voting rights to the acquiror. On the other hand, the tender offeror can avoid making a tender offer for shares of the Indiana corporation altogether even though a change in corporate control and the installation of new management would be in the best economic interests of both the tender offeror and the shareholders of the target company.

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[10] In describing the convoluted steps tender offerors can take to satisfy both federal and state requirements, Indiana, albeit unwittingly, concedes that the Control Share Chapter has a direct and substantial impact on tender offers and is far from the innocuous regulation of voting rights that it characterizes the Chapter elsewhere in its brief.

IV. THE CONTROL SHARE CHAPTER VIOLATES THE COMMERCE CLAUSE

The Control Share Chapter is per se violative of the Commerce Clause because it is designed to insulate Indiana companies from the market for corporate control, has a discriminatory effect on interstate commerce, and directly regulates economic transactions between out-of-state shareholders and tender offerors. The Chapter also violates the Commerce Clause because its burden on interstate commerce greatly outweighs its putative local benefits.

A. The Chapter is Designed to Discriminate Against Interstate Commerce

State statutes that are designed to isolate local interests from interstate markets are per se violative of the Commerce Clause. *See Philadelphia v. New Jersey,* 437 U.S. 617, 624 (1978). The Control Share Chapter is silent as to its purposes but this Court need not speculate about those purposes. Counsel of record for CTS has flatly stated that the Chapter is *intended* to insulate Indiana corporations from the interstate market for corporate control by deterring nonresidents from acquiring control of Indiana corporations:

> When asked why Indiana had decided to adopt such a virulent statute [the Control Share Chapter], James Strain, an Indianapolis corporate lawyer from Barnes and Thornburg says, "We don't like having all our companies taken over by East Coast firms." On further reflection, Strain says Midwestern and West Coast acquirors are no better.

3 *Corporate Control Alert* 1, 10 (March 1986). (App. 141) Appellants have adduced no evidence to the contrary. In fact, Indiana concedes that the Chapter is a "regulation of [corporate] takeovers." (Ind. Br. at 28)

The circumstances of Indiana's adoption of the Control Share Chapter highlight its illegitimacy. The Chapter was

passed in response to bids by nonresidents for two large Indiana corporations. 3 *Corporate Control Alert* 1, 10-11 (March 1986) (App. 141-42). The Chapter also comes in the context of a determined effort by some states to circumvent *MITE* with a new wave of anti-takeover legislation. *See generally* Block, Barton & Roth, *State Takeover Statutes: The "Second Generation,"* 13 Sec. Reg. L. J. 332 (1986). (App. 145) The most common "second generation" anti-takeover legislation has been control share acquisition statutes similar to Indiana's in both operation and effect. *Id.* Such statutes have been stricken by every court to have considered their constitutionality. *See Fleet Aerospace Corp. v. Holderman,* Fed. Sec. L. Rep. (CCH) ¶ 92,800 (6th Cir. June 25, 1986) (Ohio statute); *Terry v. Yamashita,* Fed. Sec. L. Rep. (CCH) ¶ 92,845 (D. Haw. June 13, 1986) (Hawaii statute); *APL Limited Partnership v. Van Dusen Air, Inc.,* 622 F. Supp. 1216 (D. Minn. 1985), *vacated on other grounds and appeal dismissed,* Nos. 85-5285/5286-MN (8th Cir. November 26, 1985) (Minnesota statute); *Icahn v. Blunt,* 612 F. Supp. 1400 (W.D. Mo. 1985)(Missouri statute).

B. The Chapter Has A Discriminatory Effect On Interstate Commerce

A state statute is per se violative of the Commerce Clause if it has a discriminatory effect on interstate commerce. *See Bacchus Imports, Ltd. v. Dias,* 468 U.S. 263 (1984). This Court has repeatedly emphasized that in Commerce Clause cases "[t]he principal focus of inquiry must be the practical operation of the statute, since the validity of state laws must be judged chiefly in terms of their probable effects." *Lewis v. BT Investment Managers, Inc.,* 447 U.S. 27, 37 (1980).

Appellants would have this Court consider the Control Share Chapter in a vacuum, ignoring its practical effect of discrimination against interstate commerce. Because of the distribution of financial resources in this country the large

majority of tender offers for Indiana corporations will come from out-of-state bidders and will be addressed to a sizeable majority of out-of-state shareholders. Thus, by placing a major obstacle in the way of tender offers, the Chapter inevitably disrupts the flow of interstate commerce in the market for corporate control and disproportionately burdens out-of-state acquirors and shareholders with the cost of protecting Indiana companies from takeovers.

The facial neutrality of the Control Share Chapter is thus irrelevant. This case is no different from numerous decisions of this Court under the Commerce Clause striking down facially neutral regulations as disproportionally affecting out-of-state parties and impeding the flow of interstate commerce. *See, e.g., Southern Pacific Co. v. Arizona,* 325 U.S. 761 (1945) (facially neutral regulation of train lengths).

States may not prevent out-of-state parties from gaining access to and placing in interstate commerce the resources of that state. *See, e.g., Hughes v. Oklahoma,* 441 U.S. 322 (1979) (prohibition on shipment of minnows outside state); *Pennsylvania v. West Virginia,* 262 U.S. 553 (1923) (requirement that local natural gas producers supply all in-state needs before servicing out-of-state customers). The Control Share Chapter attempts to prevent the shift of corporate control, assets and operations from Indiana to other states. For purposes of Commerce Clause analysis, it is no different from the statute in *Hughes* that prohibited the shipment of Oklahoma's minnows to other states.

The Chapter also gives the incumbent management of Indiana businesses a privileged position in the interstate market for corporate control, thereby having a discriminatory effect on interstate commerce. *Cf. Brown-Forman Distillers Corp. v. New York State Liquor Authority,* 476 U.S. ____, 106 S. Ct. 2080, 2085, 90 L.Ed 2d 552, 560 (1986) ("Economic protectionism . . . may include attempts to give local consumers an advantage over consumers in other States.") Management is free to

acquire out-of-state corporations and shift their assets and operations to Indiana. Nothing in Indiana law prevents the management of Indiana corporations from voluntarily transferring corporate control, assets and operations to other states. Yet, the Chapter allows management to strip acquirors—a large majority of whom will be from out-of-state—of the competitive advantages they may have earned for themselves in the market for corporate control by blocking them from using a tender offer which fully complies with federal law to acquire control over Indiana corporations. *See Hunt v. Washington State Apple Advertising Comm.,* 432 U.S. 333, 351 (1977). This lack of reciprocity in the Chapter portends a wave of protectionist legislation that is inconsistent with the Commerce Clause as each state attempts to restrict out-of-state acquirors from obtaining control of resident corporations while giving resident corporations free rein to obtain control of out-of-state corporations. *See generally H.P. Hood & Sons, Inc. v. DuMond,* 336 U.S. 525, 538-39 (1949).

Finally, the Control Share Chapter is unconstitutional because it forces economic operations to be performed within Indiana, even though these same operations might be performed more efficiently elsewhere if Indiana had not chilled the market for corporate control by harshly restricting tender offers. *See Pike v. Bruce Church, Inc.,* 397 U.S. 137 (1970) (striking down statute requiring cantaloupes to be packed in state; announcing rule of per se invalidity); *Toomer v. Witsell,* 334 U.S. 385 (1948) (striking down statute requiring in-state processing of shrimp); *Foster-Fountain Packing Co. v. Haydel,* 278 U.S. 1 (1928)(same).

C. The Chapter is a Direct Regulation of Interstate Commerce

The Control Share Chapter is also per se violative of the Commerce Clause because it directly regulates the transactions of out-of-state residents in interstate commerce. Last term, this

Court in *Brown-Forman Distillers, supra,* struck down as a direct regulation of interstate commerce a statute that forced liquor distillers to conform the prices they charged in other states to their in-state prices and expressly relied upon *MITE*'s discussion of the per se invalidity of direct regulations of interstate commerce, 457 U.S. at 641-643.

Like the Illinois Business Takeover Act struck down in *MITE,* the Control Share Chapter directly regulates extensive out-of-state transactions between tender offerors and shareholders by forcing the tender offeror to meet a battery of state-imposed requirements before going ahead with its tender offer. Direct regulation of nonresidents is inevitable because the Chapter applies even if the tender offeror, 90% of the target company's shareholders, and the management of the target corporation are located outside Indiana.

CTS and Indiana would have this Court believe that in adopting the Control Share Chapter, Indiana has washed its hands of any regulatory activities having extraterritorial effects. In reality Indiana has simply deputized those most likely to exploit the protectionist provisions of the Chapter: the incumbent management of Indiana corporations. Indiana's efforts are unavailing. A state may not regulate by indirection commerce within other states. *See Baldwin v. G.A.F. Seelig, Inc.,* 294 U.S. 511, 524 (1935).

D. The Chapter's Burden on Interstate Commerce Far Outweighs its Local Benefits

Even if the Control Share Chapter is not unlawful per se, it violates the Commerce Clause because the burdens it imposes on interstate commerce far exceed the putative local benefits. *See Pike v. Bruce Church, Inc.,* 397 U.S. 137, 142 (1970). Summary affirmance is warranted because this case is *MITE* revisited.

1. The Burdens on Interstate Commerce are Great

What Indiana has done with the Control Share Chapter is to "slow or freeze the flow of commerce for protectionist reasons . . . [and] . . . isolate itself from a problem common to many by erecting a barrier against the movement of interstate trade." *Philadelphia v. New Jersey,* 437 U.S. 617, 628 (1978); *see also Dean Milk Co. v. City of Madison,* 340 U.S. 349, 354 (1951)(state may not erect economic barrier to protect local industry). Indiana has burdened the interstate market for corporate control by hindering the operation of a key component of that market—the tender offer mechanism.

The impact of the Control Share Chapter on interstate commerce is indistinguishable from the impact of the Illinois Business Takeover Act struck down in *MITE.* Like the Illinois statute, the Chapter imposes an additional layer of burdensome requirements on the extensive federal regulation of tender offers. These requirements embody a strong pro-management bias and would deter numerous tender offer transactions in interstate commerce between nonresident parties.

This Court has already recognized the harm to shareholders and society when a State burdens the market for corporate control by discouraging tender offers:

> The effects of allowing [a State] to block a nationwide tender offer are substantial. Shareholders are deprived of the opportunity to sell their shares at a premium. The reallocation of economic resources to their highest valued use, a process which can improve efficiency and competition, is hindered. The incentive the tender offer mechanism provides incumbent management to perform well so that stock prices remain high is reduced.

MITE, 457 U.S. at 643.

2. The Purported Benefits of the Chapter Are Illusory

Both Indiana and CTS disingenuously suggest that the Control Share Chapter is directed at protecting shareholders

and the public, ignoring that § 23-1-42-5 gives *management* the sole discretion to adopt and administer the Chapter. It is pure sophistry to suggest that in invoking and administering the Chapter the management of Indiana corporations will have special solicitude for Indiana shareholders and residents.

Management and shareholders have divergent interests in the takeover context. *See, e.g., Unocal Corp. v. Mesa Petroleum Co.,* 493 A.2d 946, 954-55 (Del. 1985) (noting the "omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders" in considering a tender offer). CTS management's single-minded opposition to DCA's tender offer and proxy solicitation and its rush to embrace the Control Share Chapter graphically illustrate this conflict. The Seventh Circuit observed that as a result of the defensive measures deployed by the CTS management, "[t]o buy CTS, you must buy out its management." Slip op. at 16.

Ironically, the claim that the Control Share Chapter protects shareholders by requiring shareholder voting illustrates this point. The Chapter allows *management* to adopt the Control Share Chapter *without shareholder approval,* thus giving management the nearly absolute discretion to sacrifice the well-recognized benefits of tender offers to shareholders in order to preserve its control over the corporation.

In *MITE,* this Court noted that such incongruities are "at variance with [the State's] asserted legislative purpose, and tends to undermine appellants' justification for the burdens the statute imposes on interstate commerce." *MITE,* 457 U.S. at 644. There, the statute exempted from its coverage defensive self tenders orchestrated by management. Here, management has absolute discretion in employing the Chapter. *See also Raymond Motor Transportation, Inc. v. Rice,* 434 U.S. 429, 446-47 (1978) (noting that exceptions favoring local interests undermine presumption in favor of statutory validity). Benefits

to shareholders and third parties—if present at all—are only provided incidentally by the Chapter.

Even if the interests which appellants suggest that the Control Share Chapter is designed to serve are taken at face value, they are not significantly or evenhandedly advanced by the Chapter. This Court observed in *Lewis v. BT Investment Managers, Inc.* that:

> In almost any Commerce Clause case it would be possible for a State to argue that it has an interest in bolstering local ownership, or wealth, or control of business enterprise. Yet these arguments are at odds with the general principle that the Commerce Clause prohibits a State from using its regulatory power to protect its own citizens from outside competition.

447 U.S. at 43-44.[11]

a. Protection of Shareholders

Appellants argue that the chapter protects small shareholders who choose not to tender their shares and are faced with the prospect of co-existing with a large shareholder. This argument ignores reality. The available evidence indicates that small shareholders benefit from the presence of a large shareholder, as, for example, by the aggressive monitoring of management by the large shareholder, whose sizeable investment is a powerful incentive to zealous oversight. *See* Easterbrook & Fischel, *Voting in Corporate Law,* 26 J. Law. & Econ. 395 (1983). Small shareholders also share in the premiums that result from the facilitation of corporate control

[11] *Exxon Corp. v. Governor of Maryland,* 437 U.S. 117 (1978), upon which appellants rely, is clearly distinguishable because there the statute did not restrict the flow of interstate commerce or insulate local companies from the operation of an interstate market. In contrast, the Control Share Chapter chills interstate commerce by deterring tender offers to protect local companies from the interstate market for corporate control.

transaction by the large shareholder, *see* Schleifer & Vishny, *Large Shareholders and Corporate Control,* 94 J. Pol. Econ. 461 (1986), and the value of their stock actually rises on the average after a control transaction that results in the creation of a large shareholder, *see* Bradley & Rosenzweig, *Defensive Stock Repurchases,* 99 Harv. L. Rev. 1378, 1410 (1986). The Chapter thus rests upon an unsupported fear of large shareholders. By deterring tender offers altogether, the Chapter in any event is an unreasonably heavy-handed way of protecting minority shareholders from the speculative fear of oppressive conduct by an occasional large shareholder.

In addition, the shareholder protection provisions of the Control Share Chapter duplicate those of the Williams Act. The Williams Act ensures that shareholders have all relevant information before "voting" for the tender offer (and offeror) by tendering their shares. If the tender offeror fails to provide a premium sufficient to compensate shareholders for the risks that accompany a change of control, not enough shareholders will tender their shares and the tender offer will be "voted" down.[12] The Chapter distorts shareholder choice by giving management—who would otherwise have no direct role in the tender offer—the opportunity to wield its considerable influence with shareholders in a last ditch effort to scuttle the tender offer.

Finally, Indiana has other statutes which are much more closely tailored to protect minority shareholders and which are uniformly applicable to Indiana corporations. The Business Combinations Chapter, Ind. Code § 23-1-43, for example, specifically protects minority shareholders against squeeze-out mergers. Minority shareholders are vested with dissenter's rights. Ind. Code § 23-1-44. They are further protected by the fiduciary obligations to minority shareholders that Indiana law

[12] Federal proxy regulations further protect shareholders in cases like this where the tender offeror combines a proxy solicitation campaign and a tender offer.

imposes on any party who acquires control of an Indiana corporation.

b. Shareholder Ratification of a Fundamental Corporate Change

Alternatively, CTS and Indiana argue that the Control Share Chapter is an innocuous regulation of the internal affairs of Indiana corporations that gives shareholders the right to ratify a change in the pattern of ownership of the corporation's common stock by approving or disapproving a tender offer before it is consummated. They incorrectly analogize the Control Share Chapter to provisions requiring shareholder approval of mergers, sale of corporate assets, corporate dissolutions and other fundamental changes in the *structure* of the corporation.

As this Court recognized in *MITE,* tender offers do not implicate the internal affairs of the corporation. 457 U.S. at 645-46. Tender offers are transactions in interstate commerce solely between the tender offeror and shareholders. The only issue is who will supervise the assets and operations of an otherwise unchanged corporation. In contrast, mergers, sales of assets, dissolution of the corporation and creation of new classes of stock affect the internal structure of the corporation and shareholder approval provides a crucial review of management's actions in arranging these transactions.

Moreover, the complicated voting provisions of the Control Share Chapter are democratic in appearance only. Section 23-1-42-9(b)(2) of the Chapter permits even a small minority comprised of so-called disinterested shareholders to thwart the will of the majority of all shareholders with respect to a control share transaction. In contrast, all other corporate decisions which must be ratified by shareholders under Indiana law must be approved by a simple majority of *all* shareholders, be they interested, disinterested or simply uninterested.

Dire warnings to the contrary, there is no danger that by affirming the Seventh Circuit this Court will be federalizing state corporate law. By their nature, tender offers involve

extensive interstate commerce more certainly than other corporate activities regulated by the state. Moreover, because tender offers are a relatively recent phenomena, state regulation of tender offers is neither as developed nor as engrained as other areas of state corporate law. In fact, the Williams Act was prompted largely because the paucity of state tender offer regulation left investors unprotected and because of the need for uniform regulation of tender offers in the national market for corporate control.

The Seventh Circuit properly focused on the practical impact of the Control Share Chapter on interstate commerce and its decision stands for the unremarkable proposition that state laws that unduly burden interstate commerce are unconstitutional. Because of the limited and fact-intensive nature of its analysis, the Seventh Circuit's decision does not restrict in any way Indiana's authority to regulate its corporations in ways that do not unduly burden interstate commerce.

c. Protection of Indiana Companies and Residents

The Chapter is an ineffective means of protecting either Indiana companies or citizens. If the Chapter attempts to slow the pace of takeovers by resorting to economic protectionism, it is unlawful. Even if the Chapter is not per se unconstitutional, there is no reason to believe that shareholders of Indiana corporations—most of whom can be from out-of-state—will oppose value-maximizing changes in corporate control in order to keep corporate assets and operations in Indiana. Nor is there any evidence that successful tender offerors are more likely than existing management to shift the assets and operations of Indiana corporations to other states. It is significant that the Chapter neither establishes criteria that take into account the interests of Indiana citizens nor places any limits on the out-of-state transfer of assets and operations by Indiana corporations.

V. PLENARY CONSIDERATION IS UNNECESSARY

Plenary consideration of the Seventh Circuit's decision is unnecessary. The District Court did not invalidate the Chapter

altogether but only prohibited CTS from applying the Chapter against DCA's tender offer. There is also no need to reexamine *MITE*. That decision has been consistently applied by other lower courts and is dispositive here without extension or reinterpretation.

A. The District Court's Decision Was Limited to the Particular Facts of This Case

The unique facts giving rise to this case make it an inappropriate vehicle for a sweeping review by this Court of the constitutionality of the Control Share Chapter or control share acquisition statutes generally. The timing of CTS' adoption of the Chapter and its unwillingness to hold a special shareholders meeting before the Annual Meeting created a direct conflict between the Chapter and the Williams Act and a pressing threat of irreparable harm that may be absent in other cases. Neither the District Court nor the Seventh Circuit ruled out the possibility that the Chapter could constitutionally be applied by Indiana corporations that are significantly more local in nature than CTS. Indeed, the District Court's ruling was limited to a holding that the Chapter "may not constitutionally be applied *to prevent DCA* from voting any shares acquired through its tender offer at the April 25, 1986 metting." (CTS App. at 87) (emphasis added)

B. *MITE* Is Dispositive and Has Provided Clear Guidance to the Lower Courts

MITE is controlling, and provides two solid grounds for summary affirmance: (1) the direct conflict between the timing requirements of the Control Share Chapter and the Williams Act; and (2) the burden imposed by the Chapter on interstate commerce far outweighs benefits identified *post hoc* by opposing counsel. If anything, the Chapter is more objectionable than the anti-takeover statute struck down in *MITE* because it is administered by management, which is naturally more resistant to tender offers than presumptively neutral state officials.

There is no merit to CTS' claim that plenary consideration is necessary because the lower courts are divided or confused in their application of *MITE.* (CTS Br. at 9-10) The lower courts have consistently followed *MITE* in their treatment of state regulations of corporate takeovers.

Since *MITE,* lower courts have uniformly struck down statutes that were akin to the Illinois Business Takeover Act. *See, e.g., Mesa Petroleum Co. v. Cities Service Co.,* 715 F.2d 1425 (10th Cir. 1983); *Telvest v. Bradshaw,* 697 F.2d 576 (4th Cir. 1983); *Martin-Marietta Corp. v. Bendix Corp.,* 690 F.2d 558 (6th Cir. 1982); *National City Lines, Inc. v. LLC Corp.,* 687 F.2d 1122 (8th Cir. 1982). They have also uniformly struck down control share acquisition acts, correctly recognizing that such statutes are thinly veiled evasions of *MITE. See, e.g., Fleet Aerospace Corp. v. Holderman,* Fed. Sec. L. Rep. (CCH) ¶ 92,800 (6th Cir. June 25, 1986); *Terry v. Yamashita,* Fed. Sec. L. Rep. (CCH) ¶ 92,845 (D. Haw. June 13, 1986); *APL Limited Partnership v. Van Dusen Air, Inc.,* 622 F.Supp. 1216 (D. Minn. 1985), *vacated on other ground, and appeal dismissed* Nos. 85-5285/5286 MN (8th Cir. November 26, 1985); *Icahn v. Blunt,* 612 F.Supp. 1400 (W.D. Mo. 1985).

The lower courts have been guided by two principles. First, state regulations that require an extension of tender offers beyond the twenty business day period mandated by the Williams Act create an impermissible delay that runs afoul of the Supremacy Clause. Second, state regulations that interfere with significant numbers of interstate transactions between tender offerors and nonresident shareholders directly regulate interstate commerce, smack of economic protectionism, are not offset by legitimate local benefits and are barred by the Commerce Clause. These principles provide clear standards for both courts and state legislators.

The lower courts *have* upheld state legislation that is not designed to thwart tender offers and chill the market for corporate control but to advance legitimate state interests, as

suggested by Justices Powell and Stevens in their concurrences in *MITE. See, e.g., L.P. Acquisition Co. v. Tyson,* 772 F.2d 201 (6th Cir. 1985) (upholding state regulation of a tender offer that was not subject to the requirements of the Williams Act); *Cardiff Acquisitions, Inc. v. Hatch,* 751 F.2d 906 (8th Cir. 1984) (upholding portions of the Minnesota Takeover Act because they did not unduly burden tender offerors, cause delay, or allow enforcement beyond state borders).

Given the balanced approach to state tender offer regulation taken by the lower courts, the fact-intensive nature of each case that implicates state regulations and the highly unusual circumstances of the case giving rise to this appeal, plenary review is neither necessary nor desirable.

C. DCA Is Severely Prejudiced By Further Delay

Plenary consideration could deprive DCA of its rights as CTS' largest shareholder over the next crucial months. DCA's goal from the outset has been to elect its slate of directors and oust the inefficient present management of CTS.[13] But as a practical matter, DCA cannot call a special shareholders meeting to elect a new slate of CTS directors if during the pendency of this appeal it is restrained or deterred from voting any of the shares it acquired in its tender offer and in any subsequent control share acquisition. If this Court orders plenary consideration, the pendency of the appeal could prevent DCA from voting its shares at the next CTS Annual Meeting in April, 1987, when all of CTS' directors are up for election, or at an earlier shareholders meeting that DCA has the right under Indiana law to call at any time, Ind. Code § 23-1-29-2(a)(2).

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[13] The Seventh Circuit noted that "CTS has been a troubled firm of late," slip op. at 6, pointing to its declining rate of return, attributable in part to a "series of acquisitions to which [DCA] objected and which indeed turned out to be flops," *id.* at 12. It is noteworthy that the price of CTS stock has plummeted from 44¾ to 29⅛ (8/21/86) in recent weeks.

CONCLUSION

The unanimous decision of the Seventh Circuit should be summarily affirmed.

Dated: August 25, 1986

Respectfully submitted,

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(4) (4)

Nos. 86-71 & 86-97

IN THE

Supreme Court of the United States

OCTOBER TERM 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

STATE OF INDIANA,

Intervenor-Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

APPENDIX TO MOTION OF APPELLEE DYNAMICS CORPORATION OF AMERICA TO AFFIRM

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SECTION 1. IC 23-1-17 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 17. Construction and Application.

Sec. 1. This article shall be known and may be cited as the Indiana Business Corporation Law.

Sec. 2. The general assembly has power to amend or repeal all or part of this article at any time, and all domestic and foreign corporations subject to this article are governed by the amendment or repeal.

Sec. 3. (a) After July 31, 1987, this article applies to all domestic corporations in existence on July 31, 1987, that were incorporated under IC 23-1-1 through IC 23-1-12 or any other prior law. It also applies to all corporations incorporated under IC 23-1-21.

(b) Before August 1, 1987, the provisions of IC 23-1-18 through IC 23-1-54 do not apply to any domestic corporation, except in accordance with the following:

(1) The corporation's board of directors must adopt a resolution electing to have IC 23-1-18 through IC 23-1-54 (except for IC 23-1-18-3, IC 23-1-21, and IC 23-1-53-3) apply to the corporation.

(2) The resolution must specify a date (after March 31, 1986, and before August 1, 1987) on and after which those provisions will apply to the corporation.

(3) The resolution must be filed in the office of the secretary of state before the date specified under subdivision (2).

(c) The provisions of IC 23-1-18 through IC 23-1-54 (except for IC 23-1-18-3, IC 23-1-21, and IC 23-1-53-3) apply to each domestic corporation that complies with all the conditions prescribed by subsection (b). In addition, such a corporation shall continue to comply with the requirements of

IC 23-1-8 and IC 23-3-2 until August 1, 1987, but it is not subject to the provisions of IC 23-1-1 through IC 23-1-7, IC 23-1-9 through IC 23-1-12, and IC 23-3-1.

Sec. 4. After July 31, 1987, this article applies to all foreign corporations that want to transact business in Indiana. A foreign corporation authorized to transact business in Indiana on July 31, 1987, is subject to this article but is not required to obtain a new certificate of authority to transact business under this article.

Sec. 5. Official comments may be published by the general corporation law study commission (P.L.362-1985, as amended), and, after their publication, the comments may be consulted by the courts to determine the underlying reasons, purposes, and policies of this article and may be used as a guide in its construction and application.

SECTION 6. IC 23-1-22 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 22. Powers and Purposes.

Sec. 1. (a) Every corporation incorporated under this article has the purpose of engaging in any lawful business unless a more limited purpose is set forth in the articles of incorporation.

(b) A corporation engaging in a business that is subject to regulation under another statute of this state may incorporate under this article unless provisions for incorporation of corporations engaging in that business exist under that statute.

Sec. 2. Unless its articles of incorporation provide otherwise, every corporation has perpetual duration and succession in its corporate name and has the same powers as an individual to do all things necessary or convenient to carry out its business and affairs, including without limitation power to:

(1) sue and be sued, complain and defend in its corporate name;

(2) have a corporate seal, which may be altered at will, and to use it, or a facsimile of it, by impressing or affixing it or in any other manner reproducing it (however, the use of a corporate seal or an impression thereof is not required and does not affect the validity of any instrument whatsoever, notwithstanding any other statutes);

(3) make and amend bylaws, not inconsistent with its articles of incorporation or with the laws of this state, for managing the business and regulating the affairs of the corporation;

(4) purchase, receive, lease, or otherwise acquire and own, hold, improve, use, and otherwise deal with real or personal property, or any legal or equitable interest in property, wherever located;

(5) sell, convey, mortgage, pledge, lease, exchange, and otherwise dispose of all or any part of its property;

(6) purchase, receive, subscribe for, or otherwise acquire; own, hold, vote, use, sell, mortgage, lend, pledge, or otherwise dispose of; and deal in and with shares or other interests in, or obligations of, any entity, including itself, except as otherwise prohibited by this article;

(7) make contracts and guarantees, incur liabilities, borrow money, issue its notes, bonds, and other obligations (which may be convertible into or include the option to purchase other securities of the corporation), and secure any of its obligations by mortgage or pledge of any of its property, franchises, or income;

(8) lend money, invest and reinvest its funds, and receive and hold real and personal property as security for repayment;

(9) be a promoter, partner, member, associate, or manager of any partnership, joint venture, trust, or other entity;

(10) conduct its business, locate offices and exercise the powers granted by this article within or without Indiana;

(11) elect directors, elect and appoint officers, and appoint employees and agents of the corporation, define their duties, fix their compensation, and lend them money and credit;

(12) pay pensions and establish and administer pension plans, pension trusts, profit sharing plans, share bonus plans, share option plans, welfare plans, qualified and nonqualified retirement plans, and benefit or incentive plans for any or all of its current or former directors, officers, employees, and agents;

(13) make donations for the public welfare or for charitable, scientific, or educational purposes;

(14) transact any lawful business that will aid governmental policy; and

(15) make payments or donations, or do any other act, not inconsistent with law, that furthers the business and affairs of the corporation.

Sec. 3. (a) In anticipation of or during an emergency defined in subsection (d), the board of directors of a corporation may:

(1) modify lines of succession to accommodate the incapacity of any director, officer, employee, or agent; and

(2) relocate the principal office, designate alternative principal offices or regional offices, or authorize the officers to do so.

(b) During an emergency defined in subsection (d), unless emergency bylaws provide otherwise:

(1) notice of a meeting of the board of directors need be given only to those directors whom it is practicable to reach and may be given in any practicable manner, including by publication and radio; and

(2) one (1) or more officers of the corporation present at a meeting of the board of directors may be deemed to be directors for the meeting, in order of rank and within the same rank in order of seniority, as necessary to achieve a quorum.

(c) Corporate action taken in good faith during an emergency under this section to further the ordinary business affairs of the corporation:

(1) binds the corporation; and

(2) may not be used to impose liability on a corporate director, officer, employee, or agent.

(d) An emergency exists for purposes of this section if an extraordinary event prevents a quorum of the corporation's directors from assembling in time to deal with the business for which the meeting has been or is to be called.

Sec. 4. (a) In addition to any other provision contained in its articles of incorporation or bylaws or authorized by any other provision of this article, a corporation may establish one (1) or more procedures by which it regulates transactions that would, when consummated, result in a change of control of such corporation.

(b) For purposes of this section and any procedure established under this section, "control" means:

(1) for any corporation having one hundred (100) or more shareholders, the beneficial ownership, or the direct or indirect power to direct the voting, of no less than ten percent (10%) of the voting shares of a corporation's outstanding voting shares; and

(2) for any corporation having fewer than one hundred (100) shareholders, the beneficial ownership, or the direct or indirect power to direct the voting, of no less than fifty percent (50%) of the voting shares of the corporation's outstanding voting shares.

(c) A procedure established under this section may be adopted:

(1) in a corporation's original articles of incorporation or bylaws;

(2) by amending the articles of incorporation; or

(3) notwithstanding that a vote of the shareholders would otherwise be required by any other provision of this article or the articles of incorporation for the adoption or implementation of all or any portion of the procedure, by amending the bylaws.

Sec. 5. (a) Except as provided in subsection (b), the validity of corporate action may not be challenged on the ground that the corporation lacks or lacked power to act.

(b) A corporation's power to act may be challenged:

(1) in a proceeding by a shareholder against the corporation to enjoin the act;

(2) in a proceeding by the corporation, directly, derivatively, or through a receiver, trustee, or other legal representative, against an incumbent or former director, officer, employee, or agent of the corporation; or

(3) in a proceeding by the attorney general under IC 23-1-47-1.

(c) In a shareholder's proceeding under subsection (b)(1) to enjoin an unauthorized corporate act, the court may enjoin or set aside the act, if equitable and if all affected persons are parties to the proceeding, and may award damages for loss

(other than anticipated profits) suffered by the corporation or another party because of enjoining the unauthorized act.

SECTION 13. IC 23-1-29 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 29. Meetings of Shareholders.

Sec. 1. (a) A corporation must hold a meeting of the shareholders annually at a time stated in or fixed in accordance with the bylaws.

(b) Annual shareholders' meetings may be held in or out of Indiana at the place stated in or fixed in accordance with the bylaws. If no place is stated in or fixed in accordance with the bylaws, annual meetings shall be held at the corporation's principal office.

(c) The failure to hold an annual meeting at the time stated in or fixed in accordance with a corporation's bylaws does not affect the validity of any corporate action.

(d) If the articles of incorporation or bylaws so provide, any or all shareholders may participate in an annual shareholders' meeting by, or through the use of, any means of communication by which all shareholders participating may simultaneously hear each other during the meeting. A shareholder participating in a meeting by this means is deemed to be present in person at the meeting.

Sec 2. (a) A corporation must hold a special meeting of shareholders:

(1) on call of its board of directors or the person or persons authorized to do so by the articles of incorporation or bylaws; or

(2) if the holders of at least twenty-five percent (25%) of all the votes entitled to be cast on any issue proposed to be

considered at the proposed special meeting sign, date, and deliver to the corporation's secretary one (1) or more written demands for the meeting describing the purpose or purposes for which it is to be held.

(b) If not otherwise fixed under section 7 of this chapter, the record date for determining shareholders entitled to demand a special meeting is the date the first shareholder signs the demand.

(c) Special shareholders' meetings may be held in or out of Indiana at the place stated in or fixed in accordance with the bylaws. If no place is stated or fixed in accordance with the bylaws, special meetings shall be held at the corporation's principal office.

(d) Only business within the purpose or purposes described in the meeting notice required by section 5(c) of this chapter may be conducted at a special shareholders' meeting.

(e) If the articles of incorporation or bylaws so provide, any or all shareholders may participate in a special meeting of shareholders by, or through the use of, any means of communication by which all shareholders participating may simultaneously hear each other during the meeting. A shareholder participating in a meeting by this means is deemed to be present in person at the meeting.

Sec. 3. The circuit or superior court of the county where a corporation's principal office (or, if none in Indiana, its registered office) is located may order a meeting to be held and may fix the time and place of the meeting, which shall be conducted in accordance with the corporation's articles of incorporation and bylaws:

(1) on application of any shareholder of the corporation entitled to participate in an annual meeting if an annual meeting was not held within the earlier of six (6) months after the end of the corporation's fiscal year or fifteen (15) months after its last annual meeting; or

(2) on application of a shareholder who signed a demand for a special meeting valid under section 2 of this chapter if:

(A) notice of the special meeting was not given within sixty (60) days after the date the demand was delivered to the corporation's secretary; or

(B) the special meeting was not held in accordance with the notice.

Sec. 4. (a) Action required or permitted by this article to be taken at a shareholders' meeting may be taken without a meeting if the action is taken by all the shareholders entitled to vote on the action. The action must be evidenced by one (1) or more written consents describing the action taken, signed by all the shareholders entitled to vote on the action, and delivered to the corporation for inclusion in the minutes or filing with the corporate records.

(b) If not otherwise determined under section 7 of this chapter, the record date for determining shareholders entitled to take action without a meeting is the date the first shareholder signs the consent under subsection (a).

(c) A consent signed under this section has the effect of a meeting vote and may be described as such in any document.

(d) If this article requires that notice of proposed action be given to nonvoting shareholders and the action is to be taken by unanimous consent of the voting shareholders, the corporation must give its nonvoting shareholders written notice of the proposed action at least ten (10) days before the action is taken. The notice must contain or be accompanied by the same material that, under this article, would have been required to be sent to nonvoting shareholders in a notice of meeting at which the proposed action would have been submitted to the shareholders for action.

Sec. 5. (a) A corporation shall notify shareholders of the date, time, and place of each annual and special shareholders' meeting no fewer than ten (10) nor more than sixty (60) days before the meeting date. Unless this article or the articles of incorporation require otherwise, the corporation is required to give notice only to shareholders entitled to vote at the meeting.

(b) Unless this article or the articles of incorporation require otherwise, notice of an annual meeting need not include a description of the purpose or purposes for which the meeting is called.

(c) Notice of a special meeting must include a description of the purpose or purposes for which the meeting is called.

(d) If not otherwise fixed under section 7 of this chapter, the record date for determining shareholders entitled to notice of and to vote at an annual or special shareholders' meeting is the close of business on the day before the first notice is delivered to shareholders.

(e) Unless the bylaws require otherwise, if an annual or special shareholders' meeting is adjourned to a different date, time, or place, notice need not be given of the new date, time, or place if the new date, time, or place is announced at the meeting before adjournment. If a new record date for the adjourned meeting is or must be fixed under section 7 of this chapter, however, notice of the adjourned meeting must be given under this section to persons who are shareholders as of the new record date.

Sec. 6. (a) A shareholder may waive any notice required by this article, the articles of incorporation, or bylaws before or after the date and time stated in the notice. The waiver by the shareholder entitled to the notice must be in writing and be delivered to the corporation for inclusion in the minutes or filing with the corporate records.

(b) A shareholder's attendance at a meeting:

(1) waives objection to lack of notice or defective notice of the meeting, unless the shareholder at the beginning of the meeting objects to holding the meeting or transacting business at the meeting; and

(2) waives objection to consideration of a particular matter at the meeting that is not within the purpose or purposes described in the meeting notice, unless the shareholder objects to considering the matter when it is presented.

Sec. 7. (a) The bylaws may fix or provide the manner of fixing the record date for one (1) or more voting groups in order to determine the shareholders entitled to notice of a shareholders' meeting, to demand a special meeting, to vote, or to take any other action. If the bylaws do not fix or provide for fixing a record date, the board of directors of the corporation may fix a future date as the record date.

(b) A record date fixed under this section may not be more than seventy (70) days before the meeting or action requiring a determination of shareholders.

(c) A determination of shareholders entitled to notice of or to vote at a shareholders' meeting is effective for any adjournment of the meeting unless the board of directors fixes a new record date, which it must do if the meeting is adjourned to a date more than one hundred twenty (120) days after the date fixed for the original meeting.

(d) If a court orders a meeting adjourned to a date more than one hundred twenty (120) days after the date fixed for the original meeting, it may provide that the original record date continues in effect or it may fix a new record date.

SECTION 22. IC 23-1-38 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 38. Amendment of Articles of Incorporation.

Sec. 1. (a) A corporation may amend its articles of incorporation at any time to add or change a provision that is

required or permitted to be in the articles of incorporation or to delete a provision not required to be in the articles of incorporation. Whether a provision is required or permitted to be in the articles of incorporation is determined as of the effective date of the amendment.

(b) A shareholder of the corporation does not have a vested property right resulting from any provision in the articles of incorporation, or authorized to be in the bylaws by this article or the articles of incorporation including provisions relating to management, control, capital structure, dividend entitlement, or purpose or duration of the corporation.

Sec. 2. Unless the articles of incorporation provide otherwise, a corporation's board of directors may adopt one (1) or more amendments to the corporation's articles of incorporation without shareholder action to:

(1) extend the duration of the corporation if it was incorporated at a time when limited duration was required by law;

(2) delete the names and addresses of the initial directors;

(3) delete the name and address of the initial registered agent or registered office, if a statement of change is on file with the secretary of state;

(4) change each issued and unissued authorized share of an outstanding class into a greater number of whole shares or a lesser number of whole shares and fractional shares if the corporation has only shares of that class outstanding;

(5) change the corporate name by substituting the word "corporation", "incorporated", "company", "limited", or the abbreviation "corp.", "inc.", "co.", or "ltd.", for a similar word or abbreviation in the name, or by adding, deleting, or changing a geographical attribution for the name; or

(6) make any other change expressly permitted by this article to be made without shareholder action.

Sec. 3. (a) A corporation's board of directors may propose one (1) or more amendments to the articles of incorporation for submission to the shareholders.

(b) For the amendment to be adopted:

(1) the board of directors must recommend the amendment to the shareholders unless the board of directors determines that because of conflict of interest or other special circumstances it should make no recommendation and communicates the basis for its determination to the shareholders with the amendment; and

(2) the shareholders entitled to vote on the amendment must approve the amendment as provided in subsection (e).

(c) The board of directors may condition its submission of the proposed amendment on any basis.

(d) The corporation shall notify each shareholder, whether or not entitled to vote, of the proposed shareholders' meeting in accordance with IC 23-1-29-5. The notice of meeting must also state that the purpose, or one (1) of the purposes, of the meeting is to consider the proposed amendment and must contain or be accompanied by a copy or summary of the amendment.

(e) Unless this article, the articles of incorporation, or the board of directors (acting under subsection (c)) require a greater vote or a vote by voting groups, the amendment to be adopted must be approved by:

(1) a majority of the votes entitled to be cast on the amendment by any voting group with respect to which the amendment would create dissenters' rights; and

(2) the votes required by IC 23-1-30-6 and IC 23-1-30-7 by every other voting group entitled to vote on the amendment.

Sec. 4. (a) The holders of the outstanding shares of a class are entitled to vote as a separate voting group (if shareholder voting is otherwise required by this article) on a proposed amendment if the amendment would:

(1) increase or decrease the aggregate number of authorized shares of the class;

(2) effect an exchange or reclassification of all or part of the shares of the class into shares of another class;

(3) effect an exchange or reclassification, or create the right of exchange, of all or part of the shares of another class into shares of the class;

(4) change the designation, rights, preferences, or limitations of all or part of the shares of the class;

(5) change the shares of all or part of the class into a different number of shares of the same class;

(6) create a new class of shares having rights or preferences with respect to distributions or to dissolution that are prior, superior, or substantially equal to the shares of the class;

(7) increase the rights, preferences, or number of authorized shares of any class that, after giving effect to the amendment, have rights or preferences with respect to distributions or to dissolution that are prior, superior, or substantially equal to the shares of the class;

(8) limit or deny an existing preemptive right of all or part of the shares of the class; or

(9) cancel or otherwise affect rights to distributions or dividends that have accumulated but not yet been declared on all or part of the shares of the class.

(b) If a proposed amendment would affect a series of a class of shares in one (1) or more of the ways described in subsection (a), the shares of that series are entitled to vote as a separate voting group on the proposed amendment.

(c) If a proposed amendment that entitles two (2) or more series of shares to vote as separate voting groups under this section would affect those two (2) or more series in the same or a substantially similar way, the shares of all the series so affected must vote together as a single voting group on the proposed amendment.

(d) A class or series of shares is entitled to the voting rights granted by this section although the articles of incorporation provide that the shares are nonvoting shares.

Sec. 5. If a corporation has not yet issued shares, its board of directors (or if a board of directors has not been selected, then the incorporators) may adopt one (1) or more amendments to the corporation's articles of incorporation.

Sec. 6. (a) A corporation amending its articles of incorporation shall deliver to the secretary of state for filing articles of amendment setting forth:

(1) the name of the corporation;

(2) the text of each amendment adopted;

(3) if an amendment provides for an exchange, reclassification, or cancellation of issued shares, provisions for implementing the amendment if not contained in the amendment itself;

(4) the date of each amendment's adoption;

(5) if an amendment was adopted by the incorporators or board of directors without shareholder action, a statement to that effect and that shareholder action was not required;

(6) if an amendment was approved by the shareholders:

(A) the designation, number of outstanding shares, number of votes entitled to be cast by each voting group entitled to vote separately on the amendment, and number of votes of each voting group represented at the meeting;

(B) either the total number of votes cast for and against the amendment by each voting group entitled to vote separately on the amendment or the total number of votes cast for the amendment by each voting group and a statement that the number cast for the amendment by each voting group was sufficient for approval by that voting group.

(b) If a corporation amends its articles of incorporation to change its corporate name, it may, after the amendment has become effective, file for record with the county recorder of each county in Indiana in which it has real property at the time the amendment becomes effective a file-stamped copy of the articles of amendment. The validity of a change in name is not affected by a corporation's failure to record the articles of amendment.

Sec. 7. (a) A corporation's board of directors or, if the board of directors has not been selected, the incorporators may restate its articles of incorporation at any time with or without shareholder action.

(b) The restatement may include one (1) or more amendments to the articles. If the restatement includes an amendment requiring shareholder approval, it must be adopted as provided in section 3 of this chapter.

(c) If the board of directors submits a restatement for shareholder action, the corporation shall notify each shareholder, whether or not entitled to vote, of the proposed shareholders' meeting in accordance with IC 23-1-29-5. The notice must also state that the purpose, or one (1) of the purposes, of the meeting is to consider the proposed restatement and must contain or be accompanied by a copy of the restatement that identifies any amendment or other change it would make in the articles.

(d) A corporation restating its articles of incorporation shall deliver to the secretary of state for filing articles of

restatement setting forth the name of the corporation and the text of the restated articles of incorporation together with a certificate setting forth:

(1) whether the restatement contains an amendment to the articles requiring shareholder approval and, if it does not, that the board of directors adopted the restatement; or

(2) if the restatement contains an amendment to the articles requiring shareholder approval, the information required by section 6 of this chapter.

(e) Duly adopted restated articles of incorporation supersede the original articles of incorporation and all amendments to them.

(f) The secretary of state may certify restated articles of incorporation, as the articles of incorporation currently in effect, without including the certificate information required by subsection (d).

Sec. 8. (a) A corporation's articles of incorporation may be amended without action by the board of directors or shareholders to carry out a plan of reorganization ordered or decreed by a court of competent jurisdiction under federal statute if the articles of incorporation after amendment contain only provisions required or permitted by IC 23-1-21-2.

(b) The individual or individuals designated by the court shall deliver to the secretary of state for filing articles of amendment setting forth:

(1) the name of the corporation;

(2) the text of each amendment approved by the court;

(3) the date of the court's order or decree approving the articles of amendment;

(4) the title of the reorganization proceeding in which the order or decree was entered; and

(5) a statement that the court had jurisdiction of the proceeding under federal statute.

(c) Shareholders of a corporation undergoing reorganization do not have dissenters' rights except as provided in the reorganization plan.

(d) This section does not apply after entry of a final decree in the reorganization proceeding even though the court retains jurisdiction of the proceeding for limited purposes unrelated to consummation of the reorganization plan.

Sec. 9. An amendment to articles of incorporation does not affect a cause of action existing against or in favor of the corporation, a proceeding to which the corporation is a party, or the preexisting rights of persons other than shareholders of the corporation. An amendment changing a corporation's name does not abate a proceeding brought by or against the corporation in its former name.

SECTION 26. IC 23-1-42 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 42. Control Share Acquisitions.

Sec. 1. As used in this chapter, "control shares" means shares that, except for this chapter, would have voting power with respect to shares of an issuing public corporation that, when added to all other shares of the issuing public corporation owned by a person or in respect to which that person may exercise or direct the exercise of voting power, would entitle that person, immediately after acquisition of the shares (directly or indirectly, alone or as a part of a group), to exercise or direct the exercise of the voting power of the issuing public corporation in the election of directors within any of the following ranges of voting power:

(1) One-fifth (1/5) or more but less than one-third (1/3) of all voting power.

(2) One-third (1/3) or more but less than a majority of all voting power.

(3) A majority or more of all voting power.

Sec. 2. (a) As used in this chapter, "control share acquisition" means the acquisition (directly or indirectly) by any person of ownership of, or the power to direct the exercise of voting power with respect to, issued and outstanding control shares.

(b) For purposes of this section, shares acquired within ninety (90) days or shares acquired pursuant to a plan to make a control share acquisition are considered to have been acquired in the same acquisition.

(c) For purposes of this section, a person who acquires shares in the ordinary course of business for the benefit of others in good faith and not for the purpose of circumventing this chapter has voting power only of shares in respect of which that person would be able to exercise or direct the exercise of votes without further instruction from others.

(d) The acquisition of any shares of an issuing public corporation does not constitute a control share acquisition if the acquisition is consummated in any of the following circumstances:

(1) Before January 8, 1986.

(2) Pursuant to a contract existing before January 8, 1986.

(3) Pursuant to the laws of descent and distribution.

(4) Pursuant to the satisfaction of a pledge or other security interest created in good faith and not for the purpose of circumventing this chapter.

(5) Pursuant to a merger or plan of share exchange effected in compliance with IC 23-1-40 if the issuing public corporation is a party to the agreement of merger or plan of share exchange.

(e) The acquisition of shares of an issuing public corporation in good faith and not for the purpose of circumventing this chapter by or from:

(1) any person whose voting rights had previously been authorized by shareholders in compliance with this chapter; or

(2) any person whose previous acquisition of shares of an issuing public corporation would have constituted a control share acquisition but for subsection (d);

does not constitute a control share acquisition, unless the acquisition entitles any person (directly or indirectly, alone or as a part of a group) to exercise or direct the exercise of voting power of the corporation in the election of directors in excess of the range of the voting power otherwise authorized.

Sec. 3. As used in this chapter, "interested shares" means the shares of an issuing public corporation in respect of which any of the following persons may exercise or direct the exercise of the voting power of the corporation in the election of directors:

(1) An acquiring person or member of a group with respect to a control share acquisition.

(2) Any officer of the issuing public corporation.

(3) Any employee of the issuing public corporation who is also a director of the corporation.

Sec. 4. (a) As used in this chapter, "issuing public corporation" means a corporation that has:

(1) one hundred (100) or more shareholders;

(2) its principal place of business, its principal office, or substantial assets within Indiana; and

(3) either:

(A) more than ten percent (10%) of its shareholders resident in Indiana;

(B) more than ten percent (10%) of its shares owned by Indiana residents; or

(C) ten thousand (10,000) shareholders resident in Indiana.

(b) The residence of a shareholder is presumed to be the address appearing in the records of the corporation.

(c) Shares held by banks (except as trustee or guardian), brokers or nominees shall be disregarded for purposes of calculating the percentages or numbers described in this section.

Sec. 5. Unless the corporation's articles of incorporation or bylaws provide that this chapter does not apply to control share acquisitions of shares of the corporation before the control share acquisition, control shares of an issuing public corporation acquired in a control share acquisition have only such voting rights as are conferred by section 9 of this chapter.

Sec. 6. Any person who proposes to make or has made a control share acquisition may at the person's election deliver an acquiring person statement to the issuing public corporation at the issuing public corporation's principal office. The acquiring person statement must set forth all of the following:

(1) The identity of the acquiring person and each other member of any group of which the person is a part for purposes of determining control shares.

(2) A statement that the acquiring person statement is given pursuant to this chapter.

(3) The number of shares of the issuing public corporation owned (directly or indirectly) by the acquiring person and each other member of the group.

(4) The range of voting power under which the control share acquisition falls or would, if consummated, fall.

(5) If the control share acquisition has not taken place:

(A) a description in reasonable detail of the terms of the proposed control share acquisition; and

(B) representations of the acquiring person, together with a statement in reasonable detail of the facts upon which they are based, that the proposed control share acquisition, if consummated, will not be contrary to law, and that the acquiring person has the financial capacity to make the proposed control share acquisition.

Sec. 7. (a) If the acquiring person so requests at the time of delivery of an acquiring person statement and gives an undertaking to pay the corporation's expenses of a special meeting, within ten (10) days thereafter, the directors of the issuing public corporation shall call a special meeting of shareholders of the issuing public corporation for the purpose of considering the voting rights to be accorded the shares acquired or to be acquired in the control share acquisition.

(b) Unless the acquiring person agrees in writing to another date, the special meeting of shareholders shall be held within fifty (50) days after receipt by the issuing public corporation of the request.

(c) If no request is made, the voting rights to be accorded the shares acquired in the control share acquisition shall be presented to the next special or annual meeting of shareholders.

(d) If the acquiring person so requests in writing at the time of delivery of the acquiring person statement, the special meeting must not be held sooner than thirty (30) days after receipt by the issuing public corporation of the acquiring person statement.

Sec. 8. (a) If a special meeting is requested, notice of the special meeting of shareholders shall be given as promptly as reasonably practicable by the issuing public corporation to all shareholders of record as of the record date set for the meeting, whether or not entitled to vote at the meeting.

(b) Notice of the special or annual shareholder meeting at which the voting rights are to be considered must include or be accompanied by both of the following:

(1) A copy of the acquiring person statement delivered to the issuing public corporation pursuant to this chapter.

(2) A statement by the board of directors of the corporation, authorized by its directors, of its position or recommendation, or that it is taking no position or making no recommendation, with respect to the proposed control share acquisition.

Sec. 9. (a) Control shares acquired in a control share acquisition have the same voting rights as were accorded the shares before the control share acquisition only to the extent granted by resolution approved by the shareholders of the issuing public corporation.

(b) To be approved under this section, the resolution must be approved by:

(1) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that voting group, with the holders of the outstanding shares of a class being entitled to vote as a separate voting group if the proposed control share acquisition would, if fully carried out, result in any of the changes described in IC 23-1-38-4(a); and

(2) each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that group, excluding all interested shares.

Sec. 10. (a) If authorized in a corporation's articles of incorporation or bylaws before a control share acquisition has occurred, control shares acquired in a control share acquisition with respect to which no acquiring person statement has been filed with the issuing public corporation may, at any time during the period ending sixty (60) days after the last acquisition of control shares by the acquiring person, be subject to redemption by the corporation at the fair value thereof pursuant to the procedures adopted by the corporation.

(b) Control shares acquired in a control share acquisition are not subject to redemption after an acquiring person statement has been filed unless the shares are not accorded full voting rights by the shareholders as provided in section 9 of this chapter.

Sec. 11. (a) Unless otherwise provided in a corporation's articles of incorporation or bylaws before a control share acquisition has occurred, in the event control shares acquired in a control share acquisition are accorded full voting rights and the acquiring person has acquired control shares with a majority or more of all voting power, all shareholders of the issuing public corporation have dissenters' rights as provided in this chapter.

(b) As soon as practicable after such events have occurred, the board of directors shall cause a notice to be sent to all shareholders of the corporation advising them of the facts and that they have dissenters' rights to receive the fair value of their shares pursuant to IC 23-1-44.

(c) As used in this section, "fair value" means a value not less than the highest price paid per share by the acquiring person in the control share acquisition.

SECTION 27. IC 23-1-43 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 43. Business Combinations.

Sec. 1. As used in this chapter, "affiliate" means a person that directly, or indirectly through one (1) or more intermediaries, controls, is controlled by, or is under common control with, a specified person.

Sec. 2. As used in this chapter, "announcement date", when used in reference to any business combination, means the date of the first public announcement of the final, definitive proposal for the business combination.

Sec. 3. As used in this chapter, "associate", when used to indicate a relationship with any person, means:

(1) any corporation or organization of which the person is an officer or partner or is, directly or indirectly, the beneficial owner of ten percent (10%) or more of any class of voting shares;

(2) any trust or other estate in which the person has a substantial beneficial interest or as to which the person serves as trustee or in a similar fiduciary capacity; and

(3) any relative or spouse of the person, or any relative of the spouse, who has the same home as the person.

Sec. 4. As used in this chapter, "beneficial owner", when used with respect to any shares, means a person that:

(1) individually or with or through any of its affiliates or associates, beneficially owns the shares (directly or indirectly);

(2) individually or with or through any of its affiliates or associates, has:

(A) the right to acquire the shares (whether the right is exercisable immediately or only after the passage of time) under any agreement, arrangement, or understanding (whether or not in writing), or upon the exercise of conversion rights, exchange rights, warrants or options, or otherwise (however, a person is not considered the beneficial owner of shares tendered under a tender or exchange offer made by the person or any of the person's affiliates or associates until the tendered shares are accepted for purchase or exchange); or

(B) the right to vote the shares under any agreement, arrangement, or understanding (whether or not in writing) (however, a person is not considered the beneficial owner of any shares under this clause if the

agreement, arrangement, or understanding to vote the shares arises solely from a revocable proxy or consent given in response to a proxy or consent solicitation made in accordance with the applicable regulations under the Exchange Act and is not then reportable on a Schedule 13D under the Exchange Act, or any comparable or successor report); or

(3) has any agreement, arrangement, or understanding (whether or not in writing) for the purpose of acquiring, holding, voting (except voting under a revocable proxy or consent as described in subdivision (2)(B)), or disposing of the shares with any other person that beneficially owns, or whose affiliates or associates beneficially own, directly or indirectly, the shares.

Sec. 5. As used in this chapter, "business combination", when used in reference to any resident domestic corporation and any interested shareholder of the resident domestic corporation, means any of the following:

(1) Any merger of the resident domestic corporation or any subsidiary of the resident domestic corporation with:

(A) the interested shareholder; or

(B) any other corporation (whether or not itself an interested shareholder of the resident domestic corporation) that is, or after the merger or consolidation would be, an affiliate or associate of the interested shareholder.

(2) Any sale, lease, exchange, mortgage, pledge, transfer, or other disposition (in one (1) transaction or a series or transactions) to or with the interested shareholder or any affiliate or associate of the interested shareholder of assets of the resident domestic corporation or any subsidiary of the resident domestic corporation:

(A) having an aggregate market value equal to ten percent (10%) or more of the aggregate market value of all the assets, determined on a consolidated basis, of the resident domestic corporation;

(B) having an aggregate market value equal to ten percent (10%) or more of the aggregate market value of all the outstanding shares of the resident domestic corporation; or

(C) representing ten percent (10%) or more of the earning power or net income, determined on a consolidated basis, of the resident domestic corporation.

(3) The issuance or transfer by the resident domestic corporation or any subsidiary of the resident domestic corporation (in one (1) transaction or a series of transactions) of any shares of the resident domestic corporation or any subsidiary of the resident domestic corporation that have an aggregate market value equal to five percent (5%) or more of the aggregate market value of all the outstanding shares of the resident domestic corporation to the interested shareholder or any affiliate or associate of the interested shareholder except under the exercise of warrants or rights to purchase shares offered, or a dividend or distribution paid or made, pro rata to all shareholders of the resident domestic corporation.

(4) The adoption of any plan or proposal for the liquidation or dissolution of the resident domestic corporation proposed by, or under any agreement, arrangement, or understanding (whether or not in writing) with, the interested shareholder or any affiliate or associate of the interested shareholder.

(5) Any:

(A) reclassification of securities (including without limitation any share split, share dividend, or other

distribution of shares in respect of shares, or any reverse share split);

(B) recapitalization of the resident domestic corporation;

(C) merger or consolidation of the resident domestic corporation with any subsidiary of the resident domestic corporation; or

(D) other transaction (whether or not with or into or otherwise involving the interested shareholder); proposed by, or under any agreement, arrangement, or understanding (whether or not in writing) with, the interested shareholder or any affiliate or associate of the interested shareholder, that has the effect (directly or indirectly) of increasing the proportionate share of the outstanding shares of any class or series of voting shares or securities convertible into voting shares of the resident domestic corporation or any subsidiary of the resident domestic corporation that is directly or indirectly owned by the interested shareholder or any affiliate or associate of the interested shareholder, except as a result of immaterial changes due to fractional share adjustments.

(6) Any receipt by the interested shareholder or any affiliate or associate of the interested shareholder of the benefit (directly or indirectly, except proportionately as a shareholder of the resident domestic corporation), of any loans, advances, guarantees, pledges, or other financial assistance or any tax credits or other tax advantages provided by or through the resident domestic corporation.

Sec. 6. As used in this chapter, "common stock" means any shares other than preferred shares.

Sec. 7. As used in this chapter, "consummation date", with respect to any business combination, means the date of consummation of the business combination or, in the case of a

business combination as to which a shareholder vote is taken, the later of:

(1) the business day before the vote; or

(2) twenty (20) days before the date of consummation of the business combination.

Sec. 8. (a) As used in this chapter, "control", including the terms "controlling", "controlled by", and "under common control with", means the possession (directly or indirectly) of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.

(b) A person's beneficial ownership of ten percent (10%) or more of the voting power of a corporation's outstanding voting shares creates a presumption that the person has control of the corporation.

(c) Notwithstanding subsections (a) and (b), a person is not considered to have control of a corporation if the person holds voting power, in good faith and not for the purpose of circumventing this chapter, as an agent, bank, broker, nominee, custodian, or trustee for one (1) or more beneficial owners who do not individually or as a group have control of the corporation.

Sec. 9. As used in this chapter, "Exchange Act" means the Act of Congress known as the Securities Exchange Act of 1934, as amended.

Sec. 10. (a) As used in this chapter, "interested shareholder", when used in reference to any resident domestic corporation, means any person (other than the resident domestic corporation or any subsidiary of the resident domestic corporation) that is:

(1) the beneficial owner, directly or indirectly, of ten percent (10%) or more of the voting power of the outstanding voting shares of the resident domestic corporation; or

(2) an affiliate or associate of the resident domestic corporation and at any time within the five (5) year period immediately before the date in question was the beneficial owner, directly or indirectly, of ten percent (10%) or more of the voting power of the then outstanding shares of the resident domestic corporation.

(b) For the purpose of determining whether a person is an interested shareholder, the number of voting shares of the resident domestic corporation considered to be outstanding includes shares considered to be beneficially owned by the person through application of section 4 of this chapter, but does not include any other unissued shares of voting shares of the resident domestic corporation that may be issuable under any agreement, arrangement, or understanding, or upon exercise of conversion rights, warrants or options, or otherwise.

Sec. 11. As used in this chapter, "market value", when used in reference to shares or property of any resident domestic corporation, means the following:

(1) In the case of shares, the highest closing sale price of a share during the thirty (30) day period immediately preceding the date in question on the composite tape for New York Stock Exchange listed shares, or, if the shares are not quoted on the composite tape or not listed on the New York Stock Exchange, on the principal United States securities exchange registered under the Exchange Act on which the shares are listed, or, if the shares are not listed on any such exchange, the highest closing bid quotation with respect to a share during the thirty (30) day period preceding the date in question on the National Association of Securities Dealers, Inc. Automated Quotations System or any system then in use, or if no such quotation is available, the fair market value on the date in question of a share as determined by the board of directors of the resident domestic corporation in good faith.

(2) In the case of property other than cash or shares, the fair market value of the property on the date in question as determined by the board of directors of the resident domestic corporation in good faith.

Sec. 12. As used in this chapter, "preferred stock" means any class or series of shares of a resident domestic corporation that under the bylaws or articles of incorporation of the resident domestic corporation:

(1) is entitled to receive payment of dividends before any payment of dividends on some other class or series of shares; or

(2) is entitled in the event of any voluntary liquidation, dissolution, or winding up of the corporation to receive payment or distribution of a preferential amount before any payments or distributions are received by some other class or series of shares.

Sec. 13. (a) As used in this chapter, "resident domestic corporation" means a corporation that has one hundred (100) or more shareholders.

(b) A resident domestic corporation does not cease to be a resident domestic corporation by reason of events occurring or actions taken while the resident domestic corporation is subject to this chapter.

Sec. 14. As used in this chapter, "share" means:

(1) any share or similar security, any certificate of interest, any participation in any profit sharing agreement, any voting trust certificate, or any certificate of deposit for a share; and

(2) any security convertible, with or without consideration, into shares, or any warrant, call, or other option or privilege of buying shares without being bound to do so, or any other security carrying any right to acquire, subscribe to, or purchase shares.

Sec. 15. As used in this chapter, "share acquisition date", with respect to any person and any resident domestic corporation, means the date that the person first becomes an interested shareholder of the resident domestic corporation.

Sec. 16. As used in this chapter, "subsidiary" of any resident domestic corporation means any other corporation of which voting shares having a majority of the outstanding voting shares of the other corporation entitled to be cast are owned (directly or indirectly) by the resident domestic corporation.

Sec. 17. As used in this chapter, "voting shares" means shares of capital stock of a corporation entitled to vote generally in the election of directors.

Sec. 18. (a) Notwithstanding any other provision of this article (except sections 20 through 24 of this chapter), a resident domestic corporation may not engage in any business combination with any interested shareholder of the resident domestic corporation for a period of five (5) years following the interested shareholder's share acquisition date unless the business combination or the purchase of shares made by the interested shareholder on the interested shareholder's share acquisition date is approved by the board of directors of the resident domestic corporation before the interested shareholder's share acquisition date.

(b) If a good faith proposal regarding a business combination is made in writing to the board of directors of the resident domestic corporation, the board of directors shall respond, in writing, within thirty (30) days or such shorter period, if any, as may be required by the Exchange Act, setting forth its reasons for its decision regarding the proposal.

(c) If a good faith proposal to purchase shares is made in writing to the board of directors of the resident domestic corporation, the board of directors, unless it responds affirmatively in writing within thirty (30) days or such shorter period, if any, as may be required by the Exchange Act, is considered to have disapproved the share purchase.

Sec. 19. Notwithstanding any other provision of this article (except section 18 and 20 through 24 of this chapter), a resident domestic corporation may not engage at any time in any business combination with any interested shareholder of the resident domestic corporation other than a business combination meeting all requirements of the articles of incorporation of the domestic corporation and the requirements specified in any of the following:

(1) A business combination approved by the board of directors of the resident domestic corporation before the interested shareholder's share acquisition date, or as to which the purchase of shares made by the interested shareholder on the interested shareholder's share acquisition date had been approved by the board of directors of the resident domestic corporation before the interested shareholder's share acquisition date.

(2) A business combination approved by the affirmative vote of the holders of a majority of the outstanding voting shares not beneficially owned by the interested shareholder proposing the business combination, or any affiliate or associate of the interested shareholder proposing the business combination, at a meeting called for that purpose no earlier than five (5) years after the interested shareholder's share acquisition date.

(3) A business combination that meets all of the following conditions:

(A) The aggregate amount of the cash and the market value as of the consummation date of consideration other than cash to be received per share by holders of outstanding shares of common stock of the resident domestic corporation in the business combination is at least equal to the higher of the following:

(i) The highest per share price paid by the interested shareholder, at a time when the inter-

ested shareholder was the beneficial owner (directly or indirectly) of five percent (5%) or more of the outstanding voting shares of the resident domestic corporation, for any shares of common stock of the same class or series acquired by it within the five (5) year period immediately before the announcement date with respect to the business combination or within the five (5) year period immediately before, or in, the transaction in which the interested shareholder became an interested shareholder, whichever is higher; plus, in either case, interest compounded annually from the earliest date on which the highest per share acquisition price was paid through the consummation date at the rate for one (1) year United States Treasury obligations from time to time in effect; less the aggregate amount of any cash dividends paid, and the market value of any dividends paid other than in cash, per share of common stock since the earliest date, up to the amount of the interest.

(ii) The market value per share of common stock on the announcement date with respect to the business combination or on the interested shareholder's share acquisition date, whichever is higher; plus interest compounded annually from that date through the consummation date at the rate for one (1) year United States Treasury obligations from time to time in effect; less the aggregate amount of any cash dividends paid, and the market value of any dividends paid other than in cash, per share of common stock since that date, up to the amount of the interest.

(B) The aggregate amount of the cash and the market value as of the consummation date of consideration

other than cash to be received per share by holders of outstanding shares of any class or series of shares, other than common stock, of the resident domestic corporation is at least equal to the highest of the following (whether or not the interested shareholder has previously acquired any shares of the class or series of shares):

(i) The highest per share price paid by the interested shareholder, at a time when the interested shareholder was the beneficial owner (directly or indirectly) of five percent (5%) or more of the outstanding voting shares of the resident domestic corporation, for any shares of the class or series of shares acquired by it within the five (5) year period immediately before the announcement date with respect to the business combination or within the five (5) year period immediately before, or in, the transaction in which the interested shareholder became an interested shareholder, whichever is higher; plus, in either case, interest compounded annually from the earliest date on which the highest per share acquisition price was paid through the consummation date at the rate for one (1) year United States Treasury obligations from time to time in effect; less the aggregate amount of any cash dividends paid, and the market value of any dividends paid other than in cash, per share of the class or series of shares since the earliest date, up to the amount of the interest.

(ii) The highest preferential amount per share to which the holders of shares of the class or series of shares are entitled in the event of any voluntary liquidation, dissolution, or winding up of the resident domestic corporation, plus the aggregate

amount of any dividends declared or due as to which the holders are entitled before payment of dividends on some other class or series of shares (unless the aggregate amount of the dividends is included in the preferential amount).

(iii) The market value per share of the class or series of shares on the announcement date with respect to the business combination or on the interested shareholder's share acquisition date, whichever is higher; plus interest compounded annually from that date through the consummation date at the rate for one (1) year United States Treasury obligations from time to time in effect; less the aggregate amount of any cash dividends paid, and the market value of any dividends paid other than in cash, per share of the class or series of shares since that date, up to the amount of the interest.

(C) The consideration to be received by holders of a particular class or series of outstanding shares (including common stock) of the resident domestic corporation in the business combination is in cash or in the same form as the interested shareholder has used to acquire the largest number of shares of the class or series of shares previously acquired by it, and the consideration shall be distributed promptly.

(D) The holders of all outstanding shares of the resident domestic corporation not beneficially owned by the interested shareholder immediately before the consummation of the business combination are entitled to receive in the business combination cash or other consideration for the shares in compliance with clauses (A), (B), and (C).

(E) After the interested shareholder's share acquisition date and before the consummation date with respect to the business combination, the interested shareholder has not become the beneficial owner of any additional voting shares of the resident domestic corporation except:

(i) as part of the transaction that resulted in the interested shareholder becoming an interested shareholder;

(ii) by virtue of proportionate share splits, share dividends, or other distributions of shares in respect of shares not constituting a business combination under section 5(5) of this chapter;

(iii) through a business combination meeting all of the conditions of section 18 of this chapter and this section; or

(iv) through purchase by the interested shareholder at any price that, if the price had been paid in an otherwise permissible business combination the announcement date and consummation date of which were the date of the purchase, would have satisfied the requirements of clauses (A), (B), and (C).

Sec. 20. This chapter does not apply to any business combination of a resident domestic corporation that does not, as of the share acquisition date, have a class of voting shares registered with the Securities and Exchange Commission under Section 12 of the Exchange Act, unless the corporation's articles of incorporation provide otherwise.

Sec. 21. This chapter does not apply to any business combination of a resident domestic corporation the articles of incorporation of which have been amended to provide that the resident domestic corporation is subject to this chapter and that has not had a class of voting shares registered with the

Securities and Exchange Commission under Section 12 of the Exchange Act on the effective date of the amendment, and that is a business combination with an interested shareholder whose share acquisition date is before the effective date of the amendment.

Sec. 22. This chapter does not apply to any business combination of a resident domestic corporation:

(1) the original articles of incorporation of which contain a provision expressly electing not to be governed by this chapter;

(2) that, before the earlier of:

(A) September 1, 1987; or

(B) thirty (30) days after the date specified by a resolution of the board of directors adopted under IC 23-1-17-3(b), if the board of directors adopts such a resolution;

adopts an amendment to the resident domestic corporation's bylaws expressly electing not to be governed by this chapter; however, an election under this subdivision may be rescinded by subsequent amendment of the bylaws; or

(3) that adopts an amendment to the resident domestic corporation's articles of incorporation, approved by the affirmative vote of the holders, other than interested shareholders and their affiliates and associates, of a majority of the outstanding voting shares of the resident domestic corporation, excluding the voting shares of interested shareholders and their affiliates and associates, expressly electing not to be governed by this chapter, if the amendment to the articles of incorporation is not to be effective until eighteen (18) months after the vote of the resident domestic corporation's shareholders and does not apply to any business combination of the resident domestic corporation with an interested shareholder whose share acquisition date is on or before the effective date of the amendment.

Sec. 23. This chapter does not apply to any business combination of a resident domestic corporation with an interested shareholder of the resident domestic corporation who became an interested shareholder inadvertently, if the interested shareholder:

(1) as soon as practicable, divests itself of a sufficient amount of the voting shares of the corporation so that it no longer is the beneficial owner (directly or indirectly) of ten percent (10%) or more of the outstanding voting shares of the resident domestic corporation; and

(2) would not at any time within the five (5) year period preceding the announcement date with respect to the business combination have been an interested shareholder but for the inadvertent acquisition.

Sec. 24. This chapter does not apply to any business combination with an interested shareholder who was an interested shareholder on January 7, 1986.

SECTION 28. IC 23-1-44 IS ADDED TO THE INDIANA CODE AS A NEW CHAPTER TO READ AS FOLLOWS:

Chapter 44. Dissenters' Rights.

Sec. 1. As used in this chapter, "corporation" means the issuer of the shares held by a dissenter before the corporate action, or the surviving or acquiring corporation by merger or share exchange of that issuer.

Sec. 2. As used in this chapter, "dissenter" means a shareholder who is entitled to dissent from corporate action under section 8 of this chapter and who exercises that right when and in the manner required by sections 10 through 18 of this chapter.

Sec. 3. As used in this chapter, "fair value", with respect to a dissenter's shares, means the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable.

Sec. 4. As used in this chapter, "interest" means interest from the effective date of the corporate action until the date of payment, at the average rate currently paid by the corporation on its principal bank loans or, if none, at a rate that is fair and equitable under all the circumstances.

Sec. 5. As used in this chapter, "record shareholder" means the person in whose name shares are registered in the records of a corporation or the beneficial owner of shares to the extent that treatment as a record shareholder is provided under a recognition procedure or a disclosure procedure established under IC 23-1-30-4.

Sec. 6. As used in this chapter, "beneficial shareholder" means the person who is a beneficial owner of shares held by a nominee as the record shareholder.

Sec. 7. As used in this chapter, "shareholder" means the record shareholder or the beneficial shareholder.

Sec. 8. (a) A shareholder is entitled to dissent from, and obtain payment of the fair value of the shareholder's shares in the event of, any of the following corporate actions:

(1) Consummation of a plan of merger to which the corporation is a party if:

(A) shareholder approval is required for the merger by IC 23-1-40-3 or the articles of incorporation; and

(B) the shareholder is entitled to vote on the merger.

(2) Consummation of a plan of share exchange to which the corporation is a party as the corporation whose shares will be acquired, if the shareholder is entitled to vote on the plan.

(3) Consummation of a sale or exchange of all, or substantially all, of the property of the corporation other than in the usual and regular course of business, if the shareholder is entitled to vote on the sale or exchange, including a sale in dissolution, but not including a sale pursuant to court order or a sale for cash pursuant to a plan by which all or substantially all of the net proceeds of the sale will be distributed to the shareholders within one (1) year after the date of sale.

(4) The approval of a control share acquisition under IC 23-1-42.

(5) Any corporate action taken pursuant to a shareholder vote to the extent the articles of incorporation, bylaws, or a resolution of the board of directors provides that voting or nonvoting shareholders are entitled to dissent and obtain payment for their shares.

(b) This section does not apply to the holders of shares of any class or series if, on the date fixed to determine the shareholders entitled to receive notice of and vote at the meeting of shareholders at which the merger, plan of share exchange, or sale or exchange of property is to be acted on, the shares of that class or series were:

(1) registered on a United States securities exchange registered under the Exchange Act (as defined in IC 23-1-43-9); or

(2) traded on the National Association of Securities Dealers, Inc. Automated Quotations System Over-the-Counter Markets—National Market Issues or a similar market.

(c) A shareholder entitled to dissent and obtain payment for the shareholder's shares under this chapter may not chal-

lenge the corporate action creating the shareholder's entitlement.

Sec. 9. (a) A record shareholder may assert dissenters' rights as to fewer than all the shares registered in the shareholder's name only if the shareholder dissents with respect to all shares beneficially owned by any one (1) person and notifies the corporation in writing of the name and address of each person on whose behalf the shareholder asserts dissenters' rights. The rights of a partial dissenter under this subsection are determined as if the shares as to which the shareholder dissents and the shareholder's other shares were registered in the names of different shareholders.

(b) A beneficial shareholder may assert dissenters' rights as to shares held on the shareholder's behalf only if:

(1) the beneficial shareholder submits to the corporation the record shareholder's written consent to the dissent not later than the time the beneficial shareholder asserts dissenters' rights; and

(2) the beneficial shareholder does so with respect to all the beneficial shareholder's shares or those shares over which the beneficial shareholder has power to direct the vote.

Sec. 10. (a) If proposed corporate action creating dissenters' rights under section 8 of this chapter is submitted to a vote at a shareholders' meeting, the meeting notice must state that shareholders are or may be entitled to assert dissenters' rights under this chapter and be accompanied by a copy of this chapter.

(b) If corporate action creating dissenters' rights under section 8 of this chapter is taken without a vote of shareholders, the corporation shall notify in writing all shareholders entitled to assert dissenters' rights that the action was taken and send them the dissenters' notice described in section 12 of this chapter.

Sec. 11. (a) If proposed corporate action creating dissenters' rights under section 8 of this chapter is submitted to a vote at a shareholders' meeting, a shareholder who wishes to assert dissenters' rights:

(1) must deliver to the corporation before the vote is taken written notice of the shareholder's intent to demand payment for the shareholder's shares if the proposed action is effectuated; and

(2) must not vote the shareholder's shares in favor of the proposed action.

(b) A shareholder who does not satisfy the requirements of subsection (a) is not entitled to payment for the shareholder's shares under this chapter.

Sec. 12. (a) If proposed corporate action creating dissenters' rights under section 8 of this chapter is authorized at a shareholders' meeting, the corporation shall deliver a written dissenters' notice to all shareholders who satisfied the requirements of section 11 of this chapter.

(b) The dissenters' notice must be sent no later than ten (10) days after approval by the shareholders, or if corporate action is taken without approval by the shareholders, then ten (10) days after the corporate action was taken. The dissenters' notice must:

(1) state where the payment demand must be sent and where and when certificates for certificated shares must be deposited;

(2) inform holders of uncertificated shares to what extent transfer of the shares will be restricted after the payment demand is received;

(3) supply a form for demanding payment that includes the date of the first announcement to news media or to shareholders of the terms of the proposed corporate action and requires that the person asserting dissenters' rights certify whether or not the person acquired beneficial ownership of the shares before that date;

(4) set a date by which the corporation must receive the payment demand, which date may not be fewer than thirty (30) nor more than sixty (60) days after the date the subsection (a) notice is delivered; and

(5) be accompanied by a copy of this chapter.

Sec. 13. (a) A shareholder sent a dissenters' notice described in IC 23-1-42-11 or in section 12 of this chapter must demand payment, certify whether the shareholder acquired beneficial ownership of the shares before the date required to be set forth in the dissenter's notice under section 12(b)(3) of this chapter, and deposit the shareholder's certificates in accordance with the terms of the notice.

(b) The shareholder who demands payment and deposits the shareholder's shares under subsection (a) retains all other rights of a shareholder until these rights are cancelled or modified by the taking of the proposed corporate action.

(c) A shareholder who does not demand payment or deposit the shareholder's share certificates where required, each by the date set in the dissenters' notice, is not entitled to payment for the shareholder's shares under this chapter and is considered, for purposes of this article, to have voted the shareholder's shares in favor of the proposed corporate action.

Sec. 14. (a) The corporation may restrict the transfer of uncertificated shares from the date the demand for their payment is received until the proposed corporate action is taken or the restrictions released under section 16 of this chapter.

(b) The person for whom dissenters' rights are asserted as to uncertificated shares retains all other rights of a shareholder until these rights are cancelled or modified by the taking of the proposed corporate action.

Sec. 15. (a) Except as provided in section 17 of this chapter, as soon as the proposed corporate action is taken, or, if the transaction did not need shareholder approval and has been completed, upon receipt of a payment demand, the corporation shall pay each dissenter who complied with section 13 of this chapter the amount the corporation estimates to be the fair value of the dissenter's shares.

(b) The payment must be accompanied by:

(1) the corporation's balance sheet as of the end of a fiscal year ending not more than sixteen (16) months before the date of payment, an income statement for that year, a statement of changes in shareholders' equity for that year, and the latest available interim financial statements, if any;

(2) a statement of the corporation's estimate of the fair value of the shares;

(3) a statement of the dissenter's right to demand payment under section 18 of this chapter; and

(4) a copy of this chapter.

Sec. 16. (a) If the corporation does not take the proposed action within sixty (60) days after the date set for demanding payment and depositing share certificates, the corporation shall return the deposited certificates and release the transfer restrictions imposed on uncertificated shares.

(b) If after returning deposited certificates and releasing transfer restrictions, the corporation takes the proposed action, it must send a new dissenters' notice under section 12 of this chapter and repeat the payment demand procedure.

Sec. 17. (a) A corporation may elect to withhold payment required by section 15 of this chapter from a dissenter unless the dissenter was the beneficial owner of the shares before the date set forth in the dissenters' notice as the date of the first announcement to news media or to shareholders of the terms of the proposed corporate action.

(b) To the extent the corporation elects to withhold payment under subsection (a), after taking the proposed corporate action, it shall estimate the fair value of the shares and shall pay this amount to each dissenter who agrees to accept it in full satisfaction of the dissenter's demand. The corporation shall send with its offer a statement of its estimate of the fair value of the shares and a statement of the dissenter's right to demand payment under section 18 of this chapter.

Sec. 18. (a) A dissenter may notify the corporation in writing of the dissenter's own estimate of the fair value of the dissenter's shares and demand payment of the dissenter's estimate (less any payment under section 15 of this chapter), or reject the corporation's offer under section 17 of this chapter and demand payment of the fair value of the dissenter's shares, if:

(1) the dissenter believes that the amount paid under section 15 of this chapter or offered under section 17 of this chapter is less than the fair value of the dissenter's shares;

(2) the corporation fails to make payment under section 15 of this chapter within sixty (60) days after the date set for demanding payment; or

(3) the corporation, having failed to take the proposed action, does not return the deposited certificates or release the transfer restrictions imposed on uncertificated shares within sixty (60) days after the date set for demanding payment.

(b) A dissenter waives the right to demand payment under this section unless the dissenter notifies the corporation of the

dissenter's demand in writing under subsection (a) within thirty (30) days after the corporation made or offered payment for the dissenter's shares.

Sec. 19. (a) If a demand for payment under IC 23-1-42-11 or under section 18 of this chapter remains unsettled, the corporation shall commence a proceeding within sixty (60) days after receiving the payment demand and petition the court to determine the fair value of the shares. If the corporation does not commence the proceeding within the sixty (60) day period, it shall pay each dissenter whose demand remains unsettled the amount demanded.

(b) The corporation shall commence the proceeding in the circuit or superior court of the county where a corporation's principal office (or, if none in Indiana, its registered office) is located. If the corporation is a foreign corporation without a registered office in Indiana, it shall commence the proceeding in the county in Indiana where the registered office of the domestic corporation merged with or whose shares were acquired by the foreign corporation was located.

(c) The corporation shall make all dissenters (whether or not residents of this state) whose demands remain unsettled parties to the proceeding as in an action against their shares and all parties must be served with a copy of the petition. Nonresidents may be served by registered or certified mail or by publication as provided by law.

(d) The jurisdiction of the court in which the proceeding is commenced under subsection (b) is plenary and exclusive. The court may appoint one (1) or more persons as appraisers to receive evidence and recommend decision on the question of fair value. The appraisers have the powers described in the order appointing them or in any amendment to it. The dissenters are entitled to the same discovery rights as parties in other civil proceedings.

(e) Each dissenter made a party to the proceeding is entitled to judgment:

(1) for the amount, if any, by which the court finds the fair value of the dissenter's shares, plus interest, exceeds the amount paid by the corporation; or

(2) for the fair value, plus accrued interest, of the dissenter's after-acquired shares for which the corporation elected to withhold payment under section 17 of this chapter.

Sec. 20. (a) The court in an appraisal proceeding commenced under section 19 of this chapter shall determine all costs of the proceeding, including the reasonable compensation and expenses of appraisers appointed by the court. The court shall assess the costs against such parties and in such amounts as the court finds equitable.

(b) The court may also assess the fees and expenses of counsel and experts for the respective parties, in amounts the court finds equitable:

(1) against the corporation and in favor of any or all dissenters if the court finds the corporation did not substantially comply with the requirements of sections 10 through 18 of this chapter; or

(2) against either the corporation or a dissenter, in favor of any other party, if the court finds that the party against whom the fees and expenses are assessed acted arbitrarily, vexatiously, or not in good faith with respect to the rights provided by this chapter.

(c) If the court finds that the services of counsel for any dissenter were of substantial benefit to other dissenters similarly situated and that the fees for those services should not be assessed against the corporation, the court may award to these counsel reasonable fees to be paid out of the amounts awarded the dissenters who were benefited.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

DYNAMICS CORPORATION OF AMERICA,
Plaintiff,

v.

CTS CORPORATION, et al.,
Defendants.

CTS CORPORATION,
Defendant and Counterplaintiff,

v.

DYNAMICS CORPORATION OF AMERICA,
Plaintiff and Counterdefendant,

and

ANDREW LOZYNIAK, EDWARD J. MOONEY, HENRY V. KENSING, PATRICK J. DORME, FRANK A. GUNTHER, CURTIS T. ROFF, SAUL SPERBER, JOSEPH P. WALKER and HAROLD COHAN,
Additional Counterdefendants.

No. 86 C 1624
Judge Getzendanner

CTS CORPORATION'S BRIEF IN OPPOSITION TO PLAINTIFF'S REQUEST FOR A TEMPORARY RESTRAINING ORDER AND PRELIMINARY INJUNCTION AGAINST ENFORCEMENT OF THE CONTROL SHARE ACQUISITION PROVISIONS OF THE INDIANA BUSINESS CORPORATION LAW

before the control share acquisition only to the extent granted by resolution approved by the shareholders of the issuing public corporation." Before control shares are purchased, the acquiring party may (at its option) cause a special shareholder meeting to be called for the purpose of determining the voting rights of shares to be acquired in an anticipated control share acquisition. IND. CODE §§23-1-42-6, 23-1-42-7. In this case, DCA has not sought such a pre-purchase shareholder vote; thus, CTS' shareholders will decide the voting rights of DCA's control shares (if acquired) at the "next special or annual meeting of shareholders." IND. CODE §23-1-42-7(c).[3]

A resolution conferring voting rights on DCA's control shares must be approved by a majority of CTS' voting shares, excluding all interested shares. IND. CODE §23-1-42-9(b)(2). DCA's shares of CTS, as well as the shares owned by CTS' management, are within the set of "interested shares" excluded from the vote. IND. CODE §23-1-42-3. In short, before DCA's newly acquired control shares may be used to gain control of CTS' Board of Directors, DCA's control shares must be granted voting rights by a majority vote of all disinterested shares.

[3] Practical and legal barriers prevent a shareholder vote on DCA's control shares at the scheduled April 25, 1986, annual meeting of CTS' shareholders. If DCA acquires control shares, which is far from inevitable in light of the Shareholders Rights Plan adopted by CTS' Board of Directors, a special shareholder meeting for the purpose of deciding the voting rights of those control shares will have to be called.

03/31 CTS CORP.—BUSINESS SALE—2—(DJ)

ELKHART, IND. —DJ— CTS CORP., WHICH SAID IT COMPLETED THE SALE OF ITS METAL STORE FIXTURES BUSINESS TO SYNDICATE SYSTEMS INC., FOR ABOUT $28 MILLION AND WILL POST A GAIN OF $7 MILLION OR $1.25 A SHARE IN THE FIRST QUARTER FROM THE SALE, HAD YEAR-AGO FIRST QUARTER NET OF $5.9 MILLION OR $1.02 A SHARE.

SEPARATELY, THE COMPANY SAID IT HAS ELECTED TO BE GOVERNED BY THE NEW INDIANA BUSINESS CORPORATION ACT. THE COMPANY SAID, AMONG OTHER CHANGES, THE NEW ACT PROVIDES THAT THE ACQUISITION OF OVER 20 PC OF THE OUTSTANDING SHARES OF THE COMPANY, SUBJECT TO THE ACT, WILL BE A "CONTROL SHARE ACQUISITION". CTS SAID SHARES ACQUIRED IN A CONTROL SHARE ACQUISITION CANNOT BE VOTED UNTIL HOLDERS OF A MAJORITY OF THE SHARES NOT OWNED BY THE ACQUIROR AND OFFICERS OF THE COMPANY GRANT VOTING RIGHTS TO THE PURCHASER. CTS SAID IT FILED SUIT IN STATE COURT IN INDIANA, SEEKING A DECLARATION THAT THE CONTROL SHARE ACQUISITION PROVISIONS OF THE ACT ARE VALID AND ENFORCEABLE.

AS REPORTED, DYNAMICS CORP. OF AMERICA, WHICH PRESENTLY OWNS 554,600 SHARES OF CTS, RECENTLY BEGAN A PARTIAL TENDER OFFER TO BUY UP TO AN ADDITIONAL ONE MILLION SHARES OF CTS AT $43 EACH. CTS SAID IF DYNAMICS BUYS MORE THAN 575,000 SHARES UNDER THIS OFFER, THE PURCHASE WOULD BE DEFINED AS A CONTROL SHARE ACQUISITION UNDER THE ACT.

CTS ALSO SAID IT FILED A COUNTERCLAIM AGAINST DYNAMICS AND ITS DIRECTORS IN THE CASE PENDING IN FEDERAL COURT IN CHICAGO BETWEEN THE TWO COMPANIES.

CERTIFIED RESOLUTION OF THE BOARD OF DIRECTORS OF CTS CORPORATION

The undersigned officers of CTS Corporation (the "Corporation"), existing pursuant to the provisions of The Indiana General Corporation Act, as amended, desiring to give notice of corporate action effectuating application of the Indiana Business Corporation Law (except for certain provisions thereof), hereby certify that the following resolutions were duly adopted by the Board of Directors of the Corporation at a meeting thereof, duly called, constituted and held on March 27, 1986, at which a quorum of such Board of Directors were present; have not been amended or rescinded; and are in full force and effect:

> RESOLVED, That, pursuant to the procedure established in IC 23-1-17-3(b), the Board of Directors elects to have the provisions of IC 23-1-18 through IC 23-1-54 (except for IC 23-1-18-3, IC 23-1-21 and IC 23-1-53-3) apply to the Corporation on and after April 1, 1986; and
>
> RESOLVED FURTHER, That the officers of the corporation be, and the same hereby are, authorized and directed to file a certified copy of this resolution in the Office of the Secretary of State of the State of Indiana before April 1, 1986.

IN WITNESS WHEREOF, the undersigned officers execute this Certified Resolution of the Board of Directors of the Corporation, and certify to the truth of the facts herein stated, this 27th day of March, 1986.

GARY B. EREKSON	JEANNINE M. DAVIS
Gary B. Erekson Senior Vice President and Chief Financial Officer	Jeannine M. Davis Secretary and General Counsel

STATE OF INDIANA
COUNTY OF ELKHART } ss.:

I, the undersigned, a Notary Public duly commissioned to take acknowledgments and administer oaths in the State of Indiana, certify that Gary B. Erekson, Senior Vice President and Chief Financial Officer, and Jeannine M. Davis, Secretary and General Counsel, of the Corporation, the officers executing the foregoing Certified Resolution of the Board of Directors of the Corporation, personally appeared before me, acknowledged the execution thereof, and swore or attested to the truth of the facts therein stated.

WITNESS my hand and Notarial Seal this 27th day of March, 1986.

CONSTANCE P. POLLITT
Notary Public

CONSTANCE P. POLLITT
Printed Name

FILED MAR. 27, 1986

My Commission Expires: September 19, 1986

My County of Residence: Elkhart County

STATE OF INDIANA

OFFICE OF THE SECRETARY OF STATE

To Whom These Presents Come, Greeting:

WHEREAS, there has been presented to me at this office a Resolution of the Board of Directors electing to be governed by the provisions of the Indiana Business Corporation Law prior to August 1, 1987 of CTS CORPORATION and said Resolution having been prepared and signed in accordance with the provisions of the Indiana Business Corporation Law.

WHEREAS, upon due examination, I find that it satisfies the requirements of I.C. 23-1-17-3(b) and I.C. 23-1-18-1:

NOW, THEREFORE, I, EDWIN J. SIMCOX, Secretary of State of Indiana, hereby certify that I have this day filed the Resolution of the Board of Directors in this office.

Effective date the provisions will apply is April 1, 1986.

In Witness Whereof, I have hereunto set my hand and affixed the seal of the State of Indiana, at the City of Indianapolis, this 27th day of March, 1986

____

EDWIN J. SIMCOX
Secretary of State,

[Notary Seal]

By____________________
Deputy

CERTIFIED RESOLUTION OF THE BOARD OF DIRECTORS OF CTS CORPORATION

The undersigned officers of CTS Corporation (the "Corporation"), existing pursuant to the provisions of The Indiana General Corporation Act, as amended, desiring to give notice of corporate action effectuating application of the Indiana Business Corporation Law (except for certain provisions thereof), hereby certify that the following resolutions were duly adopted by the Board of Directors of the Corporation at a meeting thereof, duly called, constituted and held on March 27, 1986, at which a quorum of such Board of Directors were present; have not been amended or rescinded; and are in full force and effect:

> RESOLVED, That, pursuant to the procedure established in IC 23-1-17-3(b), the Board of Directors elects to have the provisions of IC 23-1-18 through IC 23-1-54 (except for IC 23-1-18-3, IC 23-1-21 and IC 23-1-53-3) apply to the Corporation on and after April 1, 1986; or as soon as possible after April 1, 1986, but in no event later than April 2, 1986; and
>
> RESOLVED FURTHER, That the officers of the Corporation be, and the same hereby are, authorized and directed to file a certified copy of this resolution in the Office of the Secretary of State of the State of Indiana on April 1, 1986.

IN WITNESS WHEREOF, the undersigned officers execute this Certified Resolution of the Board of Directors of the Corporation, and certify to the truth of the facts herein stated this 27th day of March, 1986.

GARY B. EREKSON	JEANNINE M. DAVIS
Gary B. Erekson Senior Vice President and Chief Financial Officer	Jeannine M. Davis Secretary and General Counsel

STATE OF INDIANA }
COUNTY OF ELKHART } SS.:

I, the undersigned, a Notary Public duly commissioned to take acknowledgments and administer oaths in the State of Indiana, certify that Gary B. Erekson, Senior Vice President and Chief Financial Officer, and Jeannine M. Davis, Secretary and General Counsel, of the Corporation, the officers executing the foregoing Certified Resolution of the Board of Directors of the Corporation, personally appeared before me, acknowledged the execution thereof, and swore or attested to the truth of the facts therein stated.

WITNESS my hand and Notarial Seal this 27th day of March, 1986.

CONSTANCE P. POLLITT
Notary Public

CONSTANCE P. POLLITT
Printed Name

FILED APR. 1, 1986

My Commission Expires: September 19, 1988

My County of Residence: Elkhart County

STATE OF INDIANA

OFFICE OF THE SECRETARY OF STATE

To Whom These Presents Come, Greeting:

WHEREAS, there has been presented to me at this office a Resolution of the Board of Directors electing to be governed by the provisions of the Indiana Business Corporation Law prior to August 1, 1987 of CTS CORPORATION and said Resolution has been prepared and signed in accordance with the provisions of the Indiana Business Corporation Law.

WHEREAS, upon due examination, I find that it satisfies the requirements of I.C. 23-1-17-3(b) and I.C. 23-1-18-1:

NOW, THEREFORE, I, EDWIN J. SIMCOX, Secretary of State of Indiana, hereby certify that I have this day filed the Resolution of the Board of Directors in this office.

Effective date the provisions will apply is April 1, 1986.

In Witness Whereof, I have hereunto set my hand and affixed the seal of the State of Indiana, at the City of Indianapolis, this 1st day of April, 1986

EDWIN J. SIMCOX
Secretary of State,

[Notary Seal]

By____________________
Deputy

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

DYNAMICS CORPORATION OF AMERICA, *Plaintiff*, vs. CTS CORPORATION, et al., *Defendants.*	DOCKET NO. 86 C 1624 Chicago, Illinois March 28, 1986 9:30 o'clock a.m.

TRANSCRIPT OF PROCEEDINGS BEFORE THE HONORABLE MILTON I. SHADUR, JUDGE

APPEARANCES:

For the Plaintiff:

MR. LOWELL E. SACHNOFF
30 South Wacker Drive, Suite 2900
Chicago, Illinois 60606

For the Defendant:

MR. STEPHEN C. SANDELS
111 West Monroe Street
Chicago, Illinois 60603

JESSE ANDREWS
Official Court Reporter—U.S. District Court
219 S. Dearborn Street
Chicago, Illinois 60604
(312) 922-5955

that is so consistent with the Williams Act and the Federal Regulation, there can not be any clearly excessive burden on Interstate Commerce in relation to local benefits.

The MITE case itself and the Securities Exchange Act of 1934, come right out and say that protecting local investors is plainly a legitimate state objective. The Securities Exchange Act states, I believe in Section 28 — it is cited on page 10 of our brief that this— that the Exchange Act is not intended to take away the regulatory powers of the authorities of State Securities Acts and State Commissioners.

THE COURT: Isn't that odd that the Indiana whatever they call it I guess they don't call it the General Assembly — the Indiana Legislature didn't talk about investors at all?

MR. SANDELS: You mean Indiana shareholders.

THE COURT: Yes.

MR. SANDELS: Let me speak to that if I may.

THE COURT: Yes.

MR. SANDELS: CTS does have about one third of its shareholders in the State of Indiana.

THE COURT: Yes I understand. I am talking about simply because their attack has been a facial attack. And, I know what you saying about standing. But you know facial attacks — Graynet (phonetically) against the City of Rockford and all that whole string of cases deal with the proposition

March 1986 Volume Three, No. 3

A report on current contests for corporate control

CORPORATE CONTROL ALERT

A publication of The American Lawyer

LEGAL DEVELOPMENTS

NEW YORK TAKEOVER STATUTE'S FIRST PROGENY

In December, when the New York legislature passed Governor Mario Cuomo's unique antitakeover legislation, several securities industry representatives predicted that other states would follow New York's lead and adopt similar statutes. It is too early to tell whether their predictions of an onslaught will prove to be correct, but Indiana has already chosen the New York approach. Also, Edward Reinfurt, vice-president of The Business Council of New York State, the principal business lobby in Albany and a strong supporter of the New York law, says that several other states have similar legislation under study.

The approach of the New York statute, which is viewed as a substantial deterrent to hostile takeovers, is to force potential acquirers of New York companies to gain the approval of the target's board before acquiring a significant stake in the company — 20% in the case of New York's law. Any acquirer that fails to get the required approval cannot do a merger, liquidate the target, acquire assets from the target, or do certain other specified transactions for five years. After five years, any contemplated transaction with the 20% holder has to be approved by holders of a majority of the outstanding shares, other than the larger holder, or meet certain fair price provisions set forth in the statute.

The statute adopted by the Indiana legislature — and awaiting the governor's signature — is substantially similar to the New York statute except that Indiana's ownership threshold is 10%. The purpose of the statute, says Paul Corsaro, a corporate specialist from Indianapolis's Bingham Summers Welsh & Spilman, is to "make it very, very difficult to take over an Indiana company."

When asked why Indiana had decided to adopt such a virulent statute, James Strain, an Indianapolis corporate lawyer from Barnes & Thornburg, says, "We don't like having all our companies taken over by East Coast firms." On further reflection, Strain says Midwestern and West Coast acquirers are no better.

In the past year, two large Indiana public companies, Hook Drugs, Inc., and Central Soya Company, Inc., were the targets of takeover bids. Hook agreed to merge with The Kroger Co. to avoid a takeover by Rite Aid Corporation, and Central Soya reached an accommodation with bidder Shamrock Holdings Inc., a private investment company owned by the Roy Disney family. There are other large public Indiana companies, including Amoco Corporation, Cummins Engine Company, Inc., and Eli Lilly and Company, that would benefit from the protection of the statute.

An Indiana lawyer familiar with the process says that the Indiana business community supported the legislation with varying degrees of enthusiasm but did not formally lobby for its passage. The impetus came primarily from the committee of Indiana lawyers appointed by the secretary of state that proposed the statute and the legislators themselves who strongly supported it. No dissenting votes were cast in either house of the legislature.

March 1986

Volume Three, No. 4 April 1986

A report on current contests for corporate control

CORPORATE CONTROL ALERT

A publication of The American Lawyer

STRATEGIES

1985—RECORD-BREAKING YEAR

The installation of a new computer system at W.T. Grimm & Co. kept the Chicago-based compiler of M&A data from disseminating its regular quarterly reports on takeover activity as 1985 progressed. So through the year, takeover lawyers and bankers had to rely on their intuition and deposit slips to tell them that 1985 was a record-breaking year. Now Grimm's new data processing system is up and running: it has finally digested the staggering quantity of data the M&A community has dished up, and the results, though not unexpected, are mind-boggling nonetheless. Here are some of the details.

In 1985, Grimm counted 3,001 transactions announced and completed or pending as of December 31, 1985. To be included in Grimm's statistics, says Tomislava Simic, Grimm's vice-president — research, a deal must have at least one U.S. party and a purchase price of $500,000 or more, and involve a formal transfer of ownership involving 10% or more of a company's equity or assets. The transactions counted include mergers, acquisitions, LBOs, and divestitures, but not open market purchases of stock. In 1985, the total purchase price of those deals was a record-breaking $179.6 billion, up 47% from 1984's $122.2 billion. Thirty-six of those deals, totaling $92.7 billion, exceeded the billion-dollar mark. That is twice the then-considered astounding 18 billion-dollar-plus deals announced in 1984. Those 36 deals totaled more than half the total value of all the 1985 deals.

In 1984, the billion-dollar deals were concentrated in the oil industry. Included were Standard Oil Company of California's $13.2 billion purchase of Gulf Oil Corporation; Texaco Inc.'s $10.1 billion purchase of Getty Oil Corp.; and Mobil Corporation's $5.7 billion purchase of Superior Oil Company. In 1985, the billion-dollar deals covered a wide range of industries, including broadcasting — the $3.5 billion purchase of American Broadcasting Companies by Capital Cities Communications Inc.; food processing — the $5.6 billion purchase of General Foods Corporation by Philip Morris Companies, Inc.; drugs and medical supplies — the $3.7 billion purchase of American Hospital Supply Corp. by Baxter Travenol Laboratories, Inc.; and aerospace — the $5 billion purchase of Hughes Aircraft Company by General Motors Corporation.

Grimm says its statistics include three "historical record breakers" among the 1985 billion-dollar deals: General Electric Company's $5.97 billion acquisition of RCA Corporation will be the largest non-oil acquisition in U.S. corporate history; the $5.36 billion buyout of Beatrice Companies, Inc. by Kohlberg Kravis Roberts & Co. will be the largest going-private transaction ever done; and Allied-Signal Inc.'s $1.7 billion divestiture of Union Texas Petroleum to a group led by Union's management and KKR is the largest unit-management buyout.

The following chart sets forth some of Grimm's findings (dollars in billions):

	1985	1984	Change
Deals completed or pending	3,001	2,543	+18%
Dollar value paid or to be paid	$179.6	$122.2	+47%
Deals over $1 billion	36	18	+100%
Dollar value of billion-dollar deals	$92.7	$58.1	+60%
Deals over $100 million	267	200	+34%
Divestitures	1,218	900	+35%
Acquisitions of public companies	336	211	+59%
Acquisitions by foreign buyers	197	151	+30%
Going-private transactions	76	57	+33%
Dollar value of going-private transactions	$24.1	$10.8	+123%
Average price/earnings ratio paid	18.0	17.2	+4.7%
Average premium for public companies	37.1%	37.9%	-2.2%

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No. 86-71

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

BRIEF OF APPELLANT CTS CORPORATION IN OPPOSITION TO MOTION TO AFFIRM

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I. INTRODUCTION.*

The Motion To Affirm ("Motion") of Dynamics Corporation of America ("DCA") is pervaded with central analytic flaw of the decision below -- namely, that because the Indiana Control Share Acquisition Chapter may make the acquisition of shares in an Indiana corporation less attractive as an economic proposition to a prospective tender offeror, the Chapter therefore "conflicts" with the Williams Act and violates the Commerce Clause. Like the Seventh Circuit, DCA ignores the fundamental differences between the Indiana statute and the Illinois statute considered in Edgar v. MITE Corp., 457 U.S. 624 (1982), and substitutes speculation about "economic impact" for analysis of the Constitutional question presented -- whether the States have the authority, in our

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*Rule 28.1 Listing: Information set forth in the Jurisdictional Statement of Appellant CTS Corporation at 1 n.1.

Federal system, to define the voting rights of shares of their domestic corporations, so long as they do not discriminate against interstate commerce. Far from demonstrating the appropriateness of summary affirmance, DCA's Motion highlights the need for plenary review.

II. DCA'S DISTORTIONS OF FACT AND LAW.

DCA's assertions that this case is "unique" and that the District Court's decision "was limited to the particular facts of this case," Motion at 25, are completely disingenuous. The Seventh Circuit's opinion, like the District Court's second (Commerce Clause) opinion, holds the Indiana statute unconstitutional on its face. It is frivolous to suggest the Chapter has any valid application under the Seventh Circuit's decision.

Equally disingenuous are DCA's references to "evidence," the statute's

"practical effect" on interstate commerce, and the "limited and fact-intensive nature" of the Seventh Circuit's analysis. E.g., Motion at 14, 15, 24. There is no factual record in this case. The District Court refused even an opportunity for an evidentiary hearing. CTS Juris. St. at 6 n.5. Like the Seventh Circuit, DCA substitutes armchair theorizing and selective law review articles for record evidence.[1]

---

[1] DCA repeatedly asserts that the Indiana statute is a "weapon" to defeat tender offers, and is "completely controlled by management." E.g., Motion at 4-6, 7-8, 19-20. In fact, the statute gives the decision whether to accord voting rights to control shares to disinterested shareholders, and excludes management. There is also no evidentiary basis for DCA's claim that the process is "controlled by management," and the statute itself gives management no opportunity to manipulate the process. The shareholder vote must be held within 50 days of receipt of the acquiring person statement; management must give prompt notice of the shareholder meeting; and the notice must include both the acquiring person's statement and a statement by the

(footnote 1 continued next page)

DCA also contends this case is MITE revisited, ignoring the patent differences between the two statutes. In the name of protecting Illinois shareholders being asked to tender their shares, the statute in MITE forbade a non-Illinois tender offeror from purchasing shares from other shareholders throughout the Nation, thus directly regulating transactions between wholly out-of-State parties. It also applied to tender offers for shares of non-Illinois corporations, thus presenting the risk of multiple and inconsistent regulations imposed upon tender offerors

(footnote 1 continued from previous page)

board of directors. IND. CODE ANN. § 23-1-42-7(b), -8 (Burns Cum. Supp. 1986). Nor does the Chapter prevent additional communications by the acquiring person to shareholders. Finally, if tender offers in fact benefit all shareholders in the corporation as DCA contends, Motion at 21-22, then one would expect the shareholders to vote for the offeror and thus facilitate hostile takeovers.

by the laws of different States. Neither is true of the Indiana statute. The Chapter applies only to Indiana corporations and it does not forbid any transactions at all, either between out-of-State parties in interstate commerce or otherwise. Rather, it regulates the post-acquisition voting power of certain shares, whether acquired in a tender offer or otherwise.[2]

[2] DCA also ignores these fundamental features of the Indiana statute in its erroneous effort to bring this case within the scope of some post-MITE lower court decisions. While some courts have struck down laws labeled "control share acquisition statutes," those statutes made the acquirer's right to purchase shares dependent on shareholder approval, and thus operated to prohibit transactions nationwide. E.g. Fleet Aerospace Corp. v. Holderman, 796 F.2d 135 (6th Cir. 1986); APL Limited Partnership v. Van Dusen Air, Inc. 622 F. Supp. 1216 (D. Minn.), vacated and appeal dismissed, Nos. 85-5285/5286MN (8th Cir. Nov. 26, 1985); Icahn v. Blunt, 612 F. Supp. 1400, 1414-20 (W.D. Mo. 1985). Indiana's statute regulates only voting rights and has utterly no effect on

(footnote 2 continued next page)

DCA also ignores this Court's divisions in MITE. It cites all portions of Justice White's opinion as a majority opinion, when in fact only Part V-B garnered five votes. For example, when DCA claims this Court "exhaustively examined the legislative history of the Williams Act," Motion at 9, the cited passage represents the views of only three Justices. Similarly, in contending that the Williams Act's so-called "policy of neutrality" not only avoids "tipping the balance" as a matter of Federal law but also preempts any State law that may affect the supposed "balance," DCA merely dismisses the contrary view, articulated

(footnote 2 continued from previous page)

an acquirer's ability to purchase shares. The court in APL recognized the importance of this distinction, stating that the voting power of control shares "once the shares have been acquired may well be a proper subject of state regulation." 622 F. Supp. at 1223-24 (emphasis in original).

by Justices Powell and Stevens and reserved by Justice O'Connor (whose votes were essential to the judgment in MITE), as an "inverted view of federalism." Motion at 11. These divisions in MITE have created uncertainty in the lower courts even as to statutes that, like the one in MITE and unlike the one here, do regulate the purchase of shares in tender offers. See CTS Juris. St. at 9-10.

III. DCA'S "CONFLICT" BETWEEN STATE AND FEDERAL LAW IS NON-EXISTENT.

DCA's purported "conflict" between the Williams Act's timing provisions for tender offer purchases and the Indiana statute's timing for a shareholder vote on control share voting rights does not exist. The State statute places no limitation on the offeror's ability to purchase. Apart from its defective premise, DCA also ignores that the Williams Act 20 business day (circa 28

calendar day) waiting period is only the minimum period during which tender offers must be kept open. 17 C.F.R. § 240.14e-1(a) (1986). Even if a tender offeror volitionally decides not to purchase shares until after the shareholder vote under the Indiana statute, it can compel that vote to occur within the permissible Williams Act period. The Chapter presents no threat of the indefinite or "extended delay" the plurality found troublesome in MITE.

Indeed, as the State of Indiana explained, a tender offeror can structure its offer so as to purchase shares after the Williams Act's minimum waiting period and without "risk" concerning the voting rights of shares it may acquire. Indiana Juris. St. at 40-46. Finally, if the only constitutional defect were the supposed "conflict" between a 28 day minimum period

for purchasing shares and a 50 day maximum period for the shareholder vote on voting rights, the State could easily repair that minor statutory detail. Instead, it is confronted with a sweeping Seventh Circuit opinion that invalidates any State law regardless of this "timing" issue.[3]

---

[3]DCA also claims its compliance with Indiana law would have been "futile" or "impossible" because, given the interplay among the timing of its partial tender offer, its proxy fight and CTS's election to be governed by the new Indiana Business Corporation Law, DCA could not vote all the shares it wanted to at the 1986 annual meeting. See Motion at 3, 9, 13. Apart from the fact that DCA could have structured its tender offer to achieve its objectives, see Indiana Juris. St. at 40-44, the entire argument is beside the point. DCA's "strategy" in a particular takeover battle is not entitled to constitutional priority over State law. Its argument rests on the novel -- and false -- assumption that it has some "Federal right" immediately to vote shares acquired in a tender offer. But State law governs shareholder meetings and voting rights -- and may provide, for example, that only shareholders of record 30 or 60 days before a meeting may vote. See, e.g., IND. CODE § 23-1-29-7 (Burns Cum. Supp.

(footnote 3 continued next page)

IV. DCA'S COMMERCE CLAUSE THEORY IS UNPRECEDENTED.

DCA concedes, as it must, that the Indiana statute regulating shareholder voting neither is limited to tender offers nor facially discriminates against interstate commerce. Motion at 6-8, 16. It therefore makes an attenuated "disproportionate impact" argument, supposedly showing a "discriminatory effect" on interstate commerce. DCA claims first that the burden of the Indiana statute "falls" most heavily "on tender offerors," and then that "the large majority of tender offers for Indiana corporations will come from out-of-state bidders and will be addressed to a sizeable majority

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(footnote 3 continued from next page)

1986) (record date may be 70 days before meeting). DCA's desire in this case to vote its shares at a particular time adds nothing to its preemption claim. Nor was that the basis of the Seventh Circuit's decision.

of out-of-state shareholders." Id. at 6-8, 15-16.

Even were these assumptions supported by record evidence (and they are not), this "disproportionate impact" theory has no foundation whatever in this Court's Commerce Clause jurisprudence. DCA's contention that this case is "no different from numerous decisions of this Court under the Commerce Clause striking down facially neutral regulations as disproportionally [sic] affecting out-of-state parties and impeding the flow of interstate commerce," Motion at 16, is accompanied by a single citation -- Southern Pacific Co. v. Arizona, 325 U.S. 761 (1945) (facially neutral regulation of train lengths). But Southern Pacific (like other transportation requirement cases) turns on the problem of multiple and conflicting State law burdens on interstate commerce. Southern Pacific

repeatedly emphasized the need for national "uniformity" and the "confusion and difficulty" that would result from conflicting State laws on train lengths. 325 U.S. at 770-71, 773-75. In this case, by contrast, one State's law must govern matters such as voting rights and shareholder approval of fundamental corporate changes. Since the Control Share Chapter applies only to Indiana corporations, there is no risk of multiple and conflicting burdens.[4]

DCA's reliance on Hughes v. Oklahoma, 441 U.S. 322 (1979), further highlights the flaw in its "discrimination" argument. In Hughes, a State statute

[4]DCA's reliance on Brown-Forman Distillers Corp. v. New York State Liquor Authority, 106 S. Ct. 2080, 90 L. Ed. 2d 552 (1986), is similarly misplaced. The State law in Brown-Forman regulated prices in wholly out-of-State transactions and plainly created a risk of multiple and conflicting burdens.

prohibited only the interstate sale of minnows and thus discriminated on its face against interstate commerce. But if the statute had instead prohibited any sale of minnows -- whether interstate or intrastate -- the mere fact that Hughes was from out-of-State could not have given him special privileges over State residents. As Justice Holmes explained long ago: "A man cannot acquire a right to property by his desire to use it in commerce among the States." Hudson County Water Co. v. McCarter, 209 U.S. 349, 357 (1908). Similarly here, the Control Share Chapter applies equally to interstate and intrastate acquisitions of the shares of Indiana corporations.

Similarly flawed is DCA's claim (citing MITE) that the Indiana statute "directly regulates" interstate commerce. Motion at 17-18. Unlike the statute in MITE, the statute here does not regulate

the purchase of shares or any other transaction in interstate commerce. This Court has never held that a statute "directly regulates" interstate commerce merely because it has some extra-territorial effects. Few if any State statutes -- and certainly no State corporation statutes -- could survive such a test. So long as the State allows out-of-State residents to own shares in its State-chartered corporations (as it constitutionally must), then any State corporation law regulating shareholder voting rights or any other internal corporate relationship will necessarily have extra-territorial effects. Like all such statutes, the one here merely defines the State-created property rights available for sale in intrastate and interstate commerce alike.

Finally, DCA's claim that the Indiana statute excessively "burdens" interstate

commerce simply perpetuates the Seventh Circuit's central error about the "interstate market for corporate control." DCA cannot deny (and so ignores) that this market exists only to the extent that State laws have created and defined the shareholder rights available for sale. Nothing in this Court's precedents requires the States to define property rights in particular ways, and nothing in the Constitution requires Indiana law inextricably to link voting rights to all other shareholder rights.[5] Absent

---

[5]DCA's stress on the importance of shareholder voting rights, e.g., Motion at 7 & n.5, is quite ironic, since State law is the source of all such rights. The "one-share, one-vote" rule, for example, is neither universal nor constitutionally required. See Providence & Worcester Co. v. Baker, 378 A.2d 121, 123 (Del. 1977) (at common law each shareholder had one vote regardless of number of shares owned). Nothing in the Constitution prohibits a "one-shareholder, one vote" rule even if it might make it more difficult for tender offerors to acquire control of corporations.

discrimination against interstate commerce, the Commerce Clause does not protect "the particular structure or methods of operation" in a market, however familiar they might be. Exxon Corp. v. Governor of Maryland, 437 U.S. 117, 127 (1978). Indeed, DCA's "interstate market for corporate control" theory is a thinly disguised variation on the "novel suggestion," rejected in Exxon, that "because the economic market for petroleum products is nationwide, no State has the power to regulate the retail marketing of gas." 437 U.S. at 128.[6]

[6]DCA's attempt to distinguish Exxon, Motion at 21 n.11, is absurd. The burden of the State law in Exxon fell "solely on [out-of-State] companies." 437 U.S. at 125 (emphasis added). Yet such effects were not unconstitutional because there was no discrimination against interstate commerce per se. Id. at 126 & n.16. Similarly, the Control Share Chapter does not discriminate against interstate commerce, even if there were evidence (i)

(footnote 6 continued next page)

DCA weakly contends the decision below will not Federalize corporation law because tender offers "involve extensive interstate commerce more certainly than other corporate activities," and "state regulation of tender offers is neither as developed nor as engrained as other areas of state corporate law." Motion at 23-24. This argument has no basis in Commerce Clause jurisprudence and also ignores the very core of the Seventh Circuit's decision. That Court concluded that the State's regulation of shareholder voting rights -- a matter as "deeply

(footnote 6 continued from next page)

that its burden "falls most heavily" on tender offerors, and (ii) that the "majority" of tender offerors will be out-of-State companies. DCA's contrary Commerce Clause theory would lead to the invalidation of countless State statutes.

engrained" as <u>any</u> "area of state corporate law" -- is unconstitutional because it makes tender offers economically less attractive. By that reasoning, <u>any</u> State corporation law that makes a corporation a less attractive takeover target is constitutionally suspect. Moreover, the suggestion that tender offers "involve extensive interstate commerce more certainly than," for example, a merger, a sale of assets, or a proxy fight, is both unsupported in the record and ridiculous.

IV. <u>CONCLUSION</u>.

This case squarely presents the question whether States are constitutionally forbidden from enacting generic corporation laws that may have the effect of making their domestic corporations less attractive as hostile takeover targets. That question is important; is not

controlled by this Court's prior decisions; and merits plenary review.

Respectfully submitted,

James A. Strain

JAMES A. STRAIN
Counsel of Record for Appellant

(6)

No. 86-71

In The

Supreme Court of the United States

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

On Appeal from the United States Court of Appeals
For the Seventh Circuit

BRIEF FOR APPELLANT CTS CORPORATION

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61P

QUESTIONS PRESENTED

1. Whether the Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE §§ 23-1-42-1 to -11 (1986), which makes the voting rights of "control shares" in covered Indiana corporations subject to a majority vote of all shareholders other than the acquiring person and incumbent management, is preempted by the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f), which regulates only disclosures to shareholders and the purchase of shares in tender offers.

2. Whether the Control Share Acquisitions Chapter, which does not discriminate against interstate commerce or out-of-state residents, applies only to Indiana corporations with other substantial ties to the State, and regulates shareholder voting rights as a matter of the State's general corporation law governing the internal affairs of Indiana corporations, is unconstitutional under the Commerce Clause.*

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* *Rule 34.1(b) and Rule 28.1 Listings:* The required information was provided in the Jurisdictional Statement of Appellant CTS Corporation at 1 n.1, and remains accurate.

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OPINIONS AND JUDGMENTS BELOW

The final opinion of the United States Court of Appeals for the Seventh Circuit (the "Seventh Circuit"), issued June 9, 1986, is published at 794 F.2d 250 and is set forth in the Appendix To Jurisdictional Statement Of Appellant CTS Corporation ("CTS App.") at A1.[1] The Seventh Circuit's judgment, entered April 23, 1986, is set forth in CTS App. at A126. The two opinions of the United States District Court for the Northern District of Illinois (the "District Court"), issued April 9 and April 16, 1986, are published together at 637 F. Supp. 389 and are set forth in CTS App. at A29 & A88. The District Court's judgment, entered April 16, 1986, is set forth in CTS App. at A138.

JURISDICTION

The judgment of the Seventh Circuit held that the Indiana Business Corporation Law's Control Share Acquisitions Chapter, IND. CODE §§23-1-42-1 to -11 (1986), was unconstitutional under the Supremacy and Commerce Clauses of the Constitution of the United States. (CTS App. at A126.) The Supreme Court has jurisdiction of this appeal pursuant to 28 U.S.C. § 1254(2). On July 16, 1986, appellant CTS Corporation ("CTS") filed in the Seventh Circuit its notice of appeal to this Court (CTS App. at A133), and the appeal was docketed in this Court on July 22, 1986, both within 90 days of the Seventh Circuit's judgment as required by 28 U.S.C. § 2101(c) and SUP. CT. R. 10.3, 12.1.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

This appeal involves the following constitutional provisions and statutes, the texts of which are set forth in

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[1] On November 17, 1986, this Court entered its order granting appellant CTS Corporation's motion to dispense with the requirement of a joint appendix in this cause.

CTS App. as indicated:

1. The Commerce Clause, U.S. CONST. art. I, § 8, cl. 3 (CTS App. at A140).
2. The Supremacy Clause, U.S. CONST. art. VI, cl. 2 (CTS App. at A140).
3. The Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (CTS App. at A141).
4. The Control Share Acquisitions Chapter, IND. CODE §§ 23-1-42-1 to -11 (1986), of the Indiana Business Corporation Law (CTS App. at A167).

STATEMENT OF THE CASE

A. General Background.

CTS is an Indiana corporation with its principal place of business in Indiana. (R. 98 at ¶ 6.)[2] Appellee Dynamics Corporation of America ("DCA") is a New York corporation with its principal place of business in Connecticut. (R. 52a at ¶ 5; R. 56a at ¶ 3.) On March 10, 1986, DCA, then the beneficial owner of approximately 9.7 percent of the outstanding shares of CTS's single class of common stock, announced a combination partial tender offer and proxy contest. (R. 98 at ¶¶ 5, 76.) DCA's tender offer sought one million shares of CTS stock, which would give it approximately 27.5 percent of the outstanding CTS shares. (R. 98 at ¶ 76.) DCA's proxy contest sought to replace CTS's board of directors with a slate proposed by DCA at CTS's annual shareholders meeting (the "Annual Meeting"), then scheduled for April 25, 1986. (R. 54a at p. 3; R. 45 at App. 3 (Schedule 14D-1); R. 98 at ¶ 16.)

On March 4, 1986, prior to DCA's announcement,

[2] Documents in the record before the Seventh Circuit in Nos. 86-1601 and 86-1608 are designated by their number on the docket sheet in the record. The record is cited here in the form "R. ___ at p. ___" or "R. ___ at ¶ ___," to indicate first, the document number and second, the page or paragraph number.

the Governor of Indiana signed into law the new Indiana Business Corporation Law, IND. CODE §§ 23-1-17-1 to 23-1-54-2 (1986), a comprehensive revision of the State's generic corporation code. Mandatory application of the new law to Indiana corporations begins August 1, 1987, but corporations may elect to be governed by it before that date. *See* IND. CODE § 23-1-17-3. On March 27, 1986, CTS elected to be covered by the new law effective April 2, 1986. (R. 52a at ¶ 103; R. 45 at pp. 35-36.) The courts below held unconstitutional the Control Share Acquisitions Chapter of the new law, IND. CODE §§ 23-1-42-1 to -11 (the "Control Share Chapter").

B. The Control Share Chapter.

The Control Share Chapter governs the voting power of "control shares" in corporations chartered under Indiana law. "Control shares" are any shares that, when added to the acquiring person's previous holdings, pass any one of three thresholds – 20, 33.3 or 50 percent – of voting strength in electing the corporation's board of directors. IND. CODE § 23-1-42-1. The Control Share Chapter applies to an "issuing public corporation," defined in IND. CODE § 23-1-42-4(a) as an Indiana corporation that has:

(1) 100 or more shareholders;

(2) its principal office, principal place of business or substantial assets in Indiana; and

(3) either more than 10 percent of its shares owned by Indiana residents, more than 10 percent of its shareholders resident in Indiana, or at least 10,000 shareholders resident in Indiana.[3]

Substantively, the Control Share Chapter does not

[3] The term "corporation" as used in the Control Share Chapter is defined for purposes of the entire Indiana Business Corporation Law as "a corporation for profit that is not a foreign corporation." IND. CODE § 23-1-20-5. Though the District Court had

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restrict or otherwise regulate the purchase or sale of control shares, whether in a tender offer or otherwise. Rather, the Chapter provides that "[c]ontrol shares acquired in a control share acquisition have the same voting rights as were accorded the shares before the control share acquisition only to the extent granted by resolution approved by the shareholders of the issuing public corporation." IND. CODE § 23-1-42-9(a). The one million shares sought (and later purchased) by DCA pursuant to its tender offer put DCA over the 20 percent threshold. Under the Control Share Chapter, therefore, the voting power of those "control shares" must be determined by a shareholder vote that excludes "all interested shares." The Chapter defines "interested shares" as shares owned by officers of the corporation, directors who are also employees of the corporation, and the acquiring person. IND. CODE §§ 23-1-42-9(b)(2) (shareholder vote) & -42-3 (defining "interested shares"). Thus, under the Chapter, DCA may not vote its newly-acquired shares until it receives a majority vote of approval by the remaining CTS shareholders who are affiliated with neither CTS management nor DCA.

The Control Share Chapter creates a mechanism for a prompt vote by the disinterested shareholders on the voting rights of the control shares. At any time before, during or after its acquisition of control shares, the acquiring person may file an "acquiring person statement" with the company. IND. CODE § 23-1-42-6. At the acquiring person's request, a special shareholders meeting to decide the voting rights of the control shares must be held no later than 50 days after the corporation receives the statement. IND. CODE § 23-1-42-7. The Control Share Chapter leaves the acquiring person free to purchase the shares either before or after the shareholder vote. If no special meeting is requested by the acquiring person, the issue will be decided at the next special or annual shareholders meeting. IND. CODE § 23-1-42-7(c). In this case, there is no indication in the record that DCA filed an acquiring person statement, requested a special meeting or ever intended to do either.

The Control Share Chapter applies to all control share acquisitions of the stock of covered Indiana corporations, regardless of the State of residency of the acquiring person. Similarly, the statute applies regardless whether the control shares are acquired in intrastate or interstate commerce, or through a tender offer, open market or private purchases, gift or otherwise.[4]

C. Proceedings In The Courts Below.

On March 10, 1986, DCA filed this action in the District Court, originally against CTS and three of its directors, alleging claims unrelated to this appeal. (R. 1.)[5] On March 27, CTS filed an action against DCA in the Superior Court of Marion County, Indiana (the "Indiana Action"), seeking a declaratory judgment that the Control

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erroneously concluded that the Control Share Chapter could be applied to foreign corporations, the Seventh Circuit corrected this error and held, as the plain language provides, that the Chapter applies only to Indiana corporations. (CTS App. at A104-05, A19.) DCA now apparently concedes that the District Court's conclusion on this issue was mistaken. (*See* Motion of Appellee Dynamics Corporation of America to Affirm ("Motion To Affirm") at 5-6.)

[4] The Chapter does not apply to control shares acquired under "the laws of descent and distribution" or in satisfaction of a pledge or security interest. IND. CODE § 23-1-42-2(d). CTS's Jurisdictional Statement at 5, 20, erroneously stated that the Chapter applies in the case of inheritance.

[5] DCA's original complaint, filed the day it announced its combination partial tender offer and proxy contest, alleged an "illegal proxy scheme" in violation of the Federal securities laws, claiming that CTS's communications to its

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Share Chapter was valid and would bar DCA from voting at the Annual Meeting any control shares it might acquire. (R. 52a at ¶¶ 115-16; R. 54a at Exhibit B.)

On March 31, 1986, four days after CTS filed the Indiana Action, DCA moved for leave to file its Third Amended Complaint in this action, adding as Count VIII a claim alleging that the Control Share Chapter is unconstitutional under (a) the Supremacy Clause, because it is allegedly preempted by the Williams Act amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (the "Williams Act"); and (b) the Commerce Clause. (R. 51a at ¶ 7; R. 52a at ¶¶ 101-17.) DCA simultaneously moved for a temporary restraining order and preliminary injunction against CTS's "enforcement" of the Control Share Chapter, including enjoining CTS from prosecuting the Indiana Action. (R. 51a.)[6] On April 4, DCA filed a supplemental memorandum stating that the relief it now sought was a judicial "declaration" that the Control Share Chapter was unconstitutional. (R. 55b at p. 1.) CTS, in addition to opposing DCA's constitutional claims on the merits, objected to any immediate decision on the constitutional issues because, *inter alia*, the Attorney

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shareholders were "designed" to "jump the gun" on the 1986 Annual Meeting and "to condition the CTS shareholders" to vote to retain the present directors. (R. 1.) Through March 27, DCA filed two amended complaints alleging additional claims and adding director defendants; CTS filed an answer and counterclaim; and the District Court denied DCA's motion for a temporary restraining order on its original claim. (R. 22, 42, 45, 39.) None of these matters is involved in the instant appeal.

[6] On April 2 and 3, 1986, District Judge Milton Shadur, acting as temporary emergency judge, heard intermittent oral argument on DCA's motions. During argument on April 3, Judge Shadur orally granted DCA's motion for leave to file its Third Amended Complaint. (*See* CTS App. at A43.) The transcript of that argument is not contained in the record on appeal.

General of Indiana had not been notified of the claim as required by 28 U.S.C. § 2403(b); no opportunity for an evidentiary hearing had been afforded; and CTS's time to answer the Third Amended Complaint had not even run. (R. 67 at pp. 5-8.)

Nevertheless, the District Court issued a Memorandum Opinion and Order on April 9, 1986, granting "DCA's motion for declaratory relief" on Count VIII of the Third Amended Complaint and ruling that the Control Share Chapter, as applied to DCA's specific plans, was preempted by the Williams Act. (CTS App. at A29, A87.) After CTS moved the District Court to certify its judgment on Count VIII as final and appealable pursuant to FED. R. CIV. P. 54(b), the District Court on April 16 *sua sponte* issued a second Memorandum Opinion and Order, which (a) stated that, if the Indiana Attorney General had been notified of the constitutional issues pursuant to 28 U.S.C. § 2403(b), the District Court would also have held the State statute unconstitutional under the Commerce Clause; (b) certified the District Court's judgment on Count VIII pursuant to Rule 54(b); and (c) "certified the appeal" of its judgment on Count VIII to the Indiana Attorney General. (CTS App. at A88, A124-25.)

CTS's appeal to the Seventh Circuit pursuant to 28 U.S.C. § 1291 was expedited in view of the imminent Annual Meeting. (CTS App. at A131.)[7] On April 23, 1986, the Seventh Circuit issued both its judgment affirming the District Court and an order briefly describing its action, stating that a full opinion would issue later.

[7] The Seventh Circuit's opinion, like its original order, erroneously states that the appeal in No. 86-1601 was pursuant to 28 U.S.C. § 1292(a)(1) (appeal of grant or denial of preliminary injunction). (CTS App. at A2, A130.) On April 17, 1986 (the day after its second opinon on the constitutional claim and the Rule 54(b) certification of its judgment on Count

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(CTS App. at A126, A129.) On June 9, 1986, the Seventh Circuit issued its final opinion, holding, *inter alia*, that the Indiana Control Share Chapter is unconstitutional both on Supremacy Clause grounds (broader than those recited by the District Court) and under the Commerce Clause.[8]

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7 *(Continued)*

VIII), the District Court had entered a preliminary injunction against CTS on DCA's separate State law claim involving a CTS shareholder rights plan, and had denied CTS's motion for a preliminary injunction against DCA based on alleged Federal securities law violations. CTS then separately appealed those District Court rulings in No. 86-1608, and the two appeals were consolidated by the Seventh Circuit. The appeal of the District Court's orders on the preliminary injunction motions (involving issues not presented to this Court) was pursuant to 28 U.S.C. § 1292(a)(1); however, the appeal of the constitutional issues presented here was from the District Court's final judgment on Count VIII (CTS App. at A124-25, A138), and was therefore pursuant to 28 U.S.C. § 1291.

[8] The following matters, while not appearing in the appellate record before the Seventh Circuit in the instant appeal, have transpired since the Seventh Circuit's judgment:

(a) On April 24, 1986, DCA purchased one million CTS shares pursuant to its tender offer and now owns approximately 27.5% of CTS's outstanding stock, thereby triggering the terms of the Control Share Chapter. *See Dynamics Corp. of America v. CTS Corp.*, 635 F. Sup. 1174, 1178 (N.D. Ill. 1986).

(b) The CTS Annual Meeting was rescheduled and held on May 16, 1986. *See Dynamics Corp. of America v. CTS Corp.*, 638 F. Supp. 802, 804 (N.D. Ill.), *aff'd in part and vacated and remanded in part*, No. 86-1888 (7th Cir. Nov. 3, 1986). All of DCA's shares were voted at the meeting, in violation of the Indiana statute but as required by the Seventh Circuit's decision. Nevertheless, DCA's proxy contest was unsuccessful and CTS's incumbent directors were re-elected. DCA then

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SUMMARY OF ARGUMENT

This case arises amid a continuing policy debate about the economic, political and social effects of hostile corporate takeovers.[9] Resolving that debate, however, is not what this case is about. Nor does this case turn on the issue presented but not definitively resolved in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982) – namely, the extent to which the States have continuing authority to regulate the purchase and sale of shares in tender offers, the subject matter of the Williams Act. Rather, the heart of this case is whether Federal law bars the States from developing their generic corporation laws in ways that do *not* restrict or regulate the purchase or sale of securities or any other transaction in interstate commerce, but that may (depending on the intentions of a potential bidder) make

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filed new claims in the District Court seeking to overturn the election, but the District Court denied DCA's request for a preliminary injunction setting aside the election results. *Dynamics Corp. of America v. CTS Corp.*, 643 F. Supp. 215 (N.D. Ill. 1986).

(c) DCA's motion for a preliminary injunction against enforcement of a second CTS shareholder rights plan was denied by the District Court in a decision that has now been partially vacated by the Seventh Circuit. *Dynamics Corp. of America v. CTS Corp.*, 638 F.Supp. 802 (N.D. Ill.), *aff'd in part and vacated and remanded in part,* No. 86-1888 (7th Cir. Nov. 3, 1986).

[9] *Compare, e.g.*, Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981), *with, e.g.*, Bebchuck, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 HARV. L. REV. 1693 (1985). In recent weeks, the debate over the merits of hostile takeover activities has intensified and has begun to shift from an academic to a Congressional forum, due to disclosures involving insider trading in takeover battles. *See, e.g.*, Ingersoll, *Political Pressures Growing to Stem Trading Excesses*, Wall St. J., Nov. 17, 1986, at 15, col. 5.

a State's domestic corporations less attractive as hostile takeover targets.

The Seventh Circuit's decision striking down the Indiana Control Share Chapter ignored the settled principles of Federalism that govern this case in favor of that court's own economic theorizing (based on *no* record evidence) about the possible impact of the Chapter on the practical calculations of a takeover bidder. Rather than focusing on the constitutional issues actually presented – *i.e.*, whether the Indiana statute in fact conflicts with the Williams Act, or in fact impermissibly burdens interstate commerce – the Seventh Circuit reasoned, in essence, that the statute is unconstitutional merely because it may make Indiana corporations less desirable as hostile takeover targets, and thereby disrupt an interstate "market for corporate control."

The Seventh Circuit's Supremacy and Commerce Clause analysis is unprecedented and its decision is wrong. With respect to preemption, there is no conflict between the provisions of the Indiana Control Share Chapter and those of the Williams Act. The Indiana statute does not even address disclosures to shareholders and the purchase and sale of securities, and it imposes no delay or other restriction whatever on a tender offeror's ability to purchase shares.

The Seventh Circuit's holding that the Control Share Chapter is preempted by the Williams Act despite the absence of any conflict between the statutes rests on a supposed policy of "neutrality" between takeover bidders and target companies inferred from isolated observations in the legislative history of the Williams Act. The "neutrality" observations, however – which at most reflect Congress's intent with respect to *Federal* law in enacting the Williams Act – are far too ambiguous to support preemption even of State statutes that, unlike the Control Share Chapter, *do* regulate the purchase and sale of securities. But even if the "neutrality" observations were a sufficient basis to

preempt some State laws dealing with the same subject matter as the Williams Act, they certainly cannot preempt State corporation laws addressed to other subjects merely because such laws may make a State's domestic corporations economically less attractive to a potential takeover bidder. The Seventh Circuit's contrary view would lead directly to the "Federalization" by the courts of vast areas of corporation law.

Nor does the Indiana Control Share Chapter violate the Commerce Clause. The Chapter does not discriminate in any way against interstate commerce. In addition, since the statute applies only to Indiana corporations with other substantial ties to the State, it poses no threat whatever of multiple and inconsistent State regulations of the same transactions. For these reasons alone, the Chapter satisfies every criteria of validity established by this Court's Commerce Clause decisions.

Even if the "balancing test" articulated in *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), were applicable here, the Control Share Chapter easily survives Commerce Clause scrutiny. The Chapter serves the legitimate State interest of protecting non-dominant shareholders in Indiana corporations by allowing them to vote on a fundamental change in the corporation – its transformation from a company owned by scattered shareholders to one controlled by a single dominant shareholder. Any extra-territorial effects of the statute are constitutionally insignificant, arising only from the fact that non-residents are also free to purchase shares of Indiana corporations. Even if the Seventh Circuit were correct in believing that the Chapter will not produce an economically efficient market for allocating corporate assets – an issue over which there is substantial academic debate and on which there is no evidence in the record – this Court has expressly rejected the view that the Commerce Clause requires the States to create economically efficient markets. *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 127-

28 (1978).

The *Exxon* holding applies with particular force when, as here, the market involves property rights that exist at all only because the State has first created and defined them in its generic corporation law. The Commerce Clause does not require the States to establish corporations at all, much less to define the property rights of a corporate share in ways that may be familiar to a given Federal court, or may be preferred by a given in-State or out-of-State investor. So long as Indiana does not discriminate against out-of-State residents or interstate commerce, it is free (as it has done in the Control Share Chapter) to define the property rights of the shares of its domestic corporations as its legislature sees fit, regardless whether that definition may make those property rights less attractive to a takeover bidder.

Neither the Seventh Circuit's disagreement with the Indiana legislature about the social and economic value of hostile takeovers nor its doubts about the policy wisdom of the Control Share Chapter render that statute unconstitutional. Contrary to the Seventh Circuit's view, the two controlling questions presented by this case involve not economics but Federalism. First, did the Congress, in enacting the Williams Act, make a political decision to bar the States from developing their generic corporation laws in ways that do *not* restrict or regulate the purchase or sale of securities, but that may make the State's domestic corporations less attractive as hostile takeover targets? Second, if the Congress made no such decision, should the "dormant " Commerce Clause nonetheless be construed to impose that same result as a matter of constitutional law?

Appellant CTS respectfully submits that the answer to both questions is "no," and that the judgment below should be reversed.

ARGUMENT

I. THE CONTROL SHARE CHAPTER IS NOT PREEMPTED BY THE WILLIAMS ACT.

The ordinary presumption of constitutionality given to State laws is strongest in the preemption context. To preserve the States' lawmaking authority, the starting assumption is "that Congress did not intend to displace state law." *Maryland v. Louisiana,* 451 U.S. 725, 746 (1981). Preemption is disfavored "in the absence of persuasive reasons – either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained." *Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co.,* 450 U.S. 311, 317 (1981). Where there is no "irreconcilable conflict" with Federal law and the nature of the subject matter does not require exclusive Federal regulation, preemption may be based only on "an unambiguous congressional mandate to that effect." *Florida Lime & Avocado Growers, Inc. v. Paul,* 373 U.S. 132, 142-47 (1963).

Because the Control Share Chapter deals only with a matter traditionally governed by State law – the voting rights of shares in Indiana corporations – the presumption against preemption in this case is especially strong. "Where . . . the field which Congress is said to have preempted has been traditionally occupied by the States, . . . 'we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'" *Jones v. Rath Packing Co.,* 430 U.S. 519, 525 (1977) (quoting *Rice v. Santa Fe Elevator Corp.,* 331 U.S. 218, 230 (1947)). Here, however, the Seventh Circuit held preempted a law that governs *only* the voting rights of shareholders in the internal affairs of corporations chartered by the State – matters *not* addressed by the Williams Act and traditionally matters of *exclusive* State concern.

A. The Williams Act Does Not Preempt State Law Absent A Direct Conflict With Federal Law, And There Is No Such Conflict In This Case.

The 1968 Williams Act added sections 13(d), 13(e), 14(d), 14(e), and 14(f), 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f), to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a to 78kk (the "Exchange Act"). The Williams Act amendments govern disclosures and statements in connection with tender offers to purchase shares, Exchange Act §§ 13(d), 14(d), 14(e) & 14(f); require or prohibit certain acts so that investors will have sufficient time to decide whether to tender their shares, *id.* §§ 13(e) & 14(d); and impose substantive requirements on tender offerors' purchases of shares, *id.* § 14(d).

None of these statutory provisions expresses *any* limit on State authority. Instead, all are subject to Section 28(a) of the Exchange Act, which provides that the Act does *not* preempt State laws that do not "conflict with" the "provisions" of the Exchange Act. 15 U.S.C. § 78bb(a). Section 28(a) "was plainly intended to protect, rather than to limit, state authority." *Leroy v. Great Western United Corp.*, 443 U.S. 173, 182 (1979).[10] Thus, the only *statutory* expression of Congressional intent is that the Williams Act is *not* intended to displace State regulation of tender offers in the absence of a direct and unavoidable conflict.

The Seventh Circuit did not base its preemption holding on any such direct conflict. The closest it came to identifying a "conflict" was its claim that, because the disinterested shareholder vote on the voting power of control shares might not take place until up to 50 days after an "acquiring person statement" is filed, a tender offeror would in practice wait beyond the 20 business day (*circa*

[10] DCA has sought to avoid the force of § 28(a), claiming that it is an old provision intended to preserve only State Blue Sky laws.

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28 calendar day) *minimum* Williams Act waiting period before purchasing the shares. The Seventh Circuit's assertion that this "impose[s] a 50-day delay on tender offers" (CTS App. at A20) is inaccurate, and there is no "conflict" with Federal law for at least three reasons.

First, the Control Share Chapter and the shareholder vote place no legal restraints whatever on the acquiring person's right to purchase shares (whether in a tender offer or otherwise), and a tender offeror is wholly free to purchase shares at *any* time permitted by the Williams Act. A legally cognizable "conflict" with Federal law cannot be manufactured by speculations about a State statute's possible impact upon a tender offeror's economic or strategic calculations – *i.e.*, its *willingness* to purchase before knowing whether the shares will be granted voting rights by disinterested shareholders.

Second, the Williams Act's approximately 28-day waiting period is only the *minimum* period a tender offer *must* be kept open. Even the maximum 50-day period for the shareholder vote under the Indiana statute is well within the Williams Act's *maximum* 60-day limit (at which time tendering shareholders must be given withdrawal rights under Federal law, 15 U.S.C. § 78n(d)(5)). Accordingly, even if speculation about a tender offeror's economic and strategic calculations could be the basis for a legal

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(Motion To Affirm at 12 n.9.) In fact, § 28(a) was amended as recently as 1982 to clarify its effect on State "bucket-shop" laws. 96 Stat. 1409 (1982). More important, the scope of § 28(a) is obviously not limited to Blue Sky laws. This Court has recognized, in language directly applicable here, that § 28(a) allows State and Federal securities regulation to "co-exist," *SEC v. National Securities, Inc.*, 393 U.S. 453, 461 (1969), and that "state law continues to apply where the [Exchange] Act itself does not," *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware*, 414 U.S. 117, 138 n.16 (1973).

"conflict" (and it cannot), there is still no conflict with the Williams Act. The Control Share Chapter poses *no* threat of the "indefinit[e]" and therefore "unreasonable" delay emphasized by Justice White in considering the Illinois statute in *MITE,* 457 U.S. 624, 637-39 (1982) (opinion of White, J.).

Third, under the Control Share Chapter, a tender offeror in fact can purchase the shares after the Williams Act's *minimum* waiting period *and* without risk concerning voting rights of the shares it acquires. As explained at greater length in the Brief for the State of Indiana, a tender offeror need only structure its offer in one of a number of possible ways so as to retain the option of returning the shares if it is later unsuccessful in acquiring voting rights.[11]

DCA takes the "conflict" argument to absurd lengths, asserting that the Chapter conflicts with the Williams Act "because it was impossible for DCA's tender offer to comply with its provisions even though [DCA] satisfied all of the requirements of the Williams Act." (Motion To Affirm at 9.) DCA's argument is wrong for each of two reasons. First and most obvious, State statutes are not preempted merely because they impose legal requirements *in addition* to those imposed by Federal law. Parallel State and Federal regulation of securities transactions, for example, has long been recognized. *See, e.g., SEC v. National Securities, Inc.,* 393 U.S. 453, 461 (1969). Rather, State laws are

[11] The parties disagree whether, under the Control Share Chapter, voting rights for DCA's control shares must be approved not only by disinterested shareholders but also by a majority of all CTS shares including "interested shares." CTS and the State of Indiana contend that IND. CODE § 23-1-42-9(b)(1) requires a second, simultaneous vote of *all* shares only where the proposed acquisition would effect certain changes in the capital structure of the company, such as changing the number of shares of stock,

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preempted only where the act of complying with Federal law *requires* violation of State law, or *vice versa. See Florida Lime & Avocado Growers,* 373 U.S. at 142-43. No such conflict is present here.

Second, DCA's "impossibility" argument involves only its particular, self-chosen strategy for taking control of CTS – namely, a partial tender offer (for approximately 17 percent of CTS's outstanding shares) *combined* with a *proxy contest* at the 1986 Annual Meeting. The "impossibility" contention has nothing to do with DCA's consummation of its *tender offer,* but rather concerns only DCA's desire to vote the acquired shares at a specific annual meeting in the context of a proxy battle it chose to initiate. Thus, any "impossibility" arose solely from DCA's choice of tactics and timing, not from any conflict between the Indiana statute and the Williams Act. A particular tender offeror's strategy in a particular takeover attempt is not entitled to constitutional priority over State law.

11 *(Continued)*
creating a new class of shares or altering the rights of a class of shares. *See* IND. CODE § 23-1-38-4(a). The District Court and Seventh Circuit disagreed; yet the District Court denied CTS's motion for *Pullman* absention on the constitutional claims, and the Seventh Circuit affirmed that denial. (CTS App. at A53-55, A19).

Assuming *arguendo* that approval by a majority of all shares is also required, this should not affect the constitutional issues. Presumably, it would be easier for DCA to win a majority of all shares since it would be able to vote its own "interested shares" in the second vote. This is particularly true since DCA alleged that its own investment in CTS stock was "enormous" while CTS's incumbent management owned but an "insignificant" amount. (R. 52a at ¶ 22.) Similarly, the Seventh Circuit observed that officers' and inside directors' "aggregate shareholdings will often be small." (CTS App. at A20.) If the constitutional issues do turn on this question of Indiana law, however, the denial of abstention was error.

Indeed, DCA's "impossibility" claim reveals the central flaw of its entire argument. At bottom, DCA's preemption theories rest on the novel – and false – assumption that it has a Federal right *immediately* to vote shares acquired in a tender offer. Patently, however, State law – *not* Federal law – governs the scheduling of and voting rights at shareholder meetings of the State's domestic corporations. For example, State law governs when shareholder meetings may be held, *e.g.*, IND. CODE § 23-1-29-1 (annual meeting must be held at time stated in or fixed in accordance with bylaws), and may provide that only shareholders of record as of a certain date may vote, *e.g.*, IND. CODE § 23-1-29-7 (bylaws or board of directors may provide for record date up to 70 days before vote). DCA's argument, however, leads to the absurd result that an annual meeting provision that did not permit a tender offeror to vote acquired shares "immediately" after the Williams Act minimum waiting period would also be preempted, or that a record date provision or any other State statute that might slow down a tender offeror's chosen timetable also impermissibly "conflicts" with Federal law. DCA's choice of tactics and timing, however, cannot create any "conflict" between the Williams Act and the Control Share Chapter; and this was not even the basis for the Seventh Circuit's decision.

B. The Control Share Chapter Is Not Preempted By Any Supposed Policy of "Neutrality" Unexpressed In The Statutory Provisions Of The Williams Act.

Rather than relying on any direct conflict between the State and Federal statutes, the Seventh Circuit based its preemption holding on its claim that the Control Share Chapter upsets "a delicate balance between the contending factions in the takeover controversy." (CTS App. at A23.) The Seventh Circuit's analysis rests on two essential premises, neither of which is correct.

The first premise is that the Williams Act implicitly

requires the States to maintain a policy of "neutrality" between incumbent management and the bidder in tender offers, and thus preempts State statutes that do not actually conflict with Federal statutory provisions but nonetheless "favor" one side or the other in the contest. That proposition is based solely on a debatable view of the legislative history of the Williams Act – a view that was accepted by three Justices in *MITE*, 457 U.S. at 634 (opinion of White, J., joined by Burger, C.J., and Blackmun, J.); rejected by two others, *id.* at 646-47, 655 (Powell, J., and Stevens, J.); and not addressed by the remaining four.

The second necessary premise is that this "neutrality" policy extends beyond the scope of the matters actually regulated by the Williams Act (*i.e.*, disclosures to shareholders and the purchase and sale of shares), and reaches other State corporation laws that may affect a bidder's practical calculations or willingness to make a hostile takeover bid. The Seventh Circuit's decision thus "Federalizes" State corporation law to the extent that any State statute will be preempted if a court concludes that it may, by some uncertain standard, "unduly" affect the desirability or outcome of either a tender offer itself or a tender offeror's post-acquisition plans for the target. Neither Justice White's opinion in *MITE* nor any lower court decision, before this one, has gone so far in extending the reach of Federal law into the internal affairs of corporations created by the States' own laws.

1. The Legislative History Of The Williams Act Does Not Support Any Preemption Of State Laws.

As noted above, there is no conflict between the Control Share Chapter and any Williams Act provision. Nor does the Williams Act itself express any Congressional intent otherwise to preempt State law. To the contrary, the pertinent provision of the Exchange Act, Section 28(a), reflects quite the opposite intention. Therefore, CTS respectfully submits at the outset that State law should

never be invalidated on the basis of a "Federal policy" discernible only, if at all, from a Federal statute's debatable legislative history.

The "political safeguards" of our Federal system require a clear and unambiguous political decision by the Congress to oust the States from legislating in an area. *See Garcia v. San Antonio Metropolitan Transit Auth.*, 469 U.S. 528, 550-55 (1985) (relying on political process to preserve State sovereignty). Such a political decision should be evident on the face of the Federal statute itself. An "unambiguous congressional mandate," *Florida Lime & Avocado Growers, Inc.*, 373 U.S. at 147, or an "unmistakabl[e]" Congressional decision, *Chicago & North Western Transportation Co.*, 450 U.S. at 317, is required. These political safeguards of our Federalism would fail of their essential purpose if courts were free to invalidate State laws on the basis of perceived "policy judgments" the Congress itself did not consider sufficiently important to enact into positive law. *Cf. Pennhurst State School and Hospital v. Halderman*, 465 U.S. 89, 99 (1984) (requiring "unequivocal expression of congressional intent" to overturn States' Eleventh Amendment immunity under Fourteenth Amendment). If this Court agrees, this is the end of the preemption issue in this case.

Furthermore, even if legislative history alone could theoretically oust the States from legislating in an area, the legislative history of the Williams Act is far too ambiguous a basis for doing so here. At most, that legislative history indicates only that the Congress did not want *Federal* law to upset the "balance between the contending factions in the takeover controversy." This simply does not support the far broader proposition of the Seventh Circuit (and of Justice White's opinion in *MITE*) that Congress at the same time implicitly prohibited the States from taking any steps that might affect that balance. Whatever the Williams Act's legislative history indicates about Congress's intentions for *Federal* policy toward takeovers,

that history provides *no* foundation for the second and far more dramatic step of preempting *State* laws in the absence of a direct conflict.

This Court's decision in *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 26-35 (1977), explained the context of the Congressional "balance." As the *Piper* Court observed, the bill as first introduced was intended to protect incumbent corporate management from cash tender offers, a strategy that had not been regulated by Federal securities laws until passage of the Williams Act. In committee hearings, however, witnesses "indicated . . . that takeover bids could often serve a useful function." *Id.* at 30. Sensitive to the suggestion that the bill would favor one side or the other in control contests, the Williams Act sponsors "made it clear that the legislation was designed solely to get needed information to the investor," *id.* at 30-31, and that they had " 'taken extreme care to avoid tipping the scales either in favor of management or in favor of the person making the takeover bids.' " *Id.* at 31 (quoting 113 Cong. Rec. 24664 (1967) (remarks of Sen. Williams)).

Placed in context, these references to neutrality on the part of *Congress* do not support the conclusion that the Williams Act also implicitly barred the *States* from affecting the "balance of power" between the tender offeror and the target:

> Congress was indeed committed to a policy of neutrality in contests for control, *but its policy of evenhandedness does not go either to the purpose of the legislation* or to whether a private cause of action is implicit in the statute. *Neutrality is, rather, but one characteristic of legislation directed toward a different purpose – the protection of investors.* Indeed, the statements concerning the need for Congress to maintain a neutral posture in takeover attempts are contained in the section of the Senate Report entitled, "Protection of Investors." Taken in their totality, these statements confirm that what Congress had in mind

> was the protection of shareholders, the "pawn[s] in a form of industrial warfare." The Senate Report expressed the purpose as "plac[ing] investors on an equal footing with the takeover bidder," Senate Report 4, without favoring either the tender offeror or existing management.

430 U.S. at 29-30 (emphasis added). Hence, the references to "neutrality" suggest only that Congress *itself* did not wish to "tip the balance" with the Williams Act, not that Congress intended the Act to be a comprehensive scheme regulating tender offers to the exclusion of State authority. The neutrality references in the legislative history thus fall far short of the "unambiguous congressional mandate" required to justify preemption.

The Seventh Circuit acknowledged that "it is a big leap from saying that the Williams Act does not itself exhibit much hostility to tender offers to saying that it implicitly forbids states to adopt more hostile regulations." (CTS App. at A22.) Nonetheless, it relied on Justice White's and its own opinions in *MITE* and on subsequent lower court decisions to justify that "big leap," stating that "whatever doubts . . . we might entertain as an original matter are stilled by the weight of precedent." (CTS App. at A23.) The "weight of precedent" is not at all persuasive here, however, because a majority of this Court has never accepted the proposition that the Williams Act forbids States from adopting any laws more hostile to takeovers.

The Seventh Circuit's further reliance on *Piper* and on *Schreiber v. Burlington Northern, Inc.*, 472 U.S. ___, 86 L. Ed. 2d 1 (1985), is plainly misplaced. In *Piper*, this Court expressly *rejected* the argument that the Williams Act created a "pervasive scheme of federal regulation of tender offers" that would support an implied cause of action, 430 U.S. at 29 – which is virtually a holding that Congress did *not* intend to oust the States from legislating in the area. *See Merrell Dow Pharmaceuticals Inc. v. Thompson*, 478 U.S. ___, 92 L. Ed. 2d 650, 662-63

& n.13 (1986). Similarly, the *Schreiber* Court *refused* to extend the Williams Act to regulate the substantive fairness of defensive strategies by the target corporation's board of directors, and instead expressly left such matters to State corporation law. There was no suggestion in *Schreiber* that the State corporation law governing defensive strategies must also display an appropriate "neutrality" lest it encroach upon the Williams Act; yet that result is logically compelled by the Seventh Circuit's decision.

In short, a majority of this Court has never held (either in *MITE* or any other case) that whatever inferences of Congressional "neutrality" can be drawn from the Williams Act's legislative history implicitly require the States to be equally "neutral" in their own legislation governing their domestic corporations. To the contrary, a majority of this Court has consistently held that neither the Williams Act nor other Federal securities statutes evince any Congressional intent to "Federalize" corporation law beyond the specific subjects those statutes address. *E.g., Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977). And in preemption cases generally, this Court has repeatedly held that Federal court invalidation of State laws on preemption grounds, one of the most sensitive areas of Federalism, requires unmistakable, unambiguous evidence that Congress so intended – evidence that the most expansive reading of the Williams Act's debatable legislative history cannot supply. For these reasons alone, the Indiana Control Share Chapter is not preempted by the Williams Act.

2. Any Preemption Under The Supposed "Neutrality Principle" Must In Any Event Be Limited To The Subject Matter Of The Williams Act, And Cannot Preempt State Corporation Laws That Do Not Regulate The Purchase And Sale Of Securities.

Even assuming that "neutrality" statements from the Williams Act's legislative history could preempt otherwise valid State laws, it still does not follow – as the Seventh Circuit effectively held – that *any* State laws making tender offers less attractive to the offeror are preempted. Rather, the scope of any preemption arising from that legislative history must be limited by the subject matter of the Williams Act.

Absent a direct conflict between State and Federal law, this Court's cases have necessarily limited preemption to those matters *actually regulated* by Federal statutes, and have not extended preemption to any State law that might touch on the area. For example, in *Huron Portland Cement Co. v. Detroit,* 362 U.S. 440, 444-46 (1960), the Court concluded that Federal laws governing inspection of steamship boilers did not preempt local air pollution regulations even though the local laws prohibited conduct allowed by Federal law. Because there was "no overlap" between the Federal and local laws, there was no preemption: "To hold otherwise would be to ignore the teaching of this Court's decisions which enjoin seeking out conflicts between state and federal regulation where none clearly exists." 362 U.S. at 446. *Accord, e.g., Rice v. Santa Fe Elevator Corp.,* 331 U.S. 218, 237 (1947) (no preemption where Federal and State laws related to different matters and any conflict was speculative).

The Williams Act and its legislative history address only a narrow subject – the interactions among tender offerors, incumbent management and investors up to the point when the investor makes an "informed choice"

whether to tender his shares. As Justice White said in *MITE*, "Congress sought to protect the investor not only by furnishing him with the necessary information but also by withholding from management or the bidder any undue advantage that could frustrate the exercise of an informed choice." 457 U.S. at 634.

The Control Share Chapter, by contrast, regulates only post-acquisition voting rights and addresses entirely different concerns. Unlike the Illinois statute in *MITE*, the Indiana statute does *not* prohibit, restrict or otherwise regulate disclosures to shareholders or the purchase and sale of shares. Instead, it allows a tender offeror or other acquiring person to purchase shares at any time permitted by Federal law, but protects the interests of other shareholders (*e.g.*, in a tender offer, the interests of shareholders who choose *not* to tender their shares) vis-a-vis a new and potentially dominant one. The Chapter is thus beyond the scope of whatever preemption might be mandated by the supposed "neutrality principle."

The Indiana legislature had legitimate reasons to be concerned with the situation where one shareholder acquires a dominant portion of voting shares. There is an inherent possibility of unfair treatment when a dominant (but not 100 percent) shareholder maintains the controlled corporation as a partly-owned subsidiary for some unspecified time. *See* Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 Harv. L. Rev. 1693, 1711 (1985) (dominant shareholder adopts such a strategy only to take "advantage of minority shareholders"). The Indiana Control Share Chapter allows dispersed shareholders in a firm with a new and potentially dominant shareholder to protect their interests by voting.

In so doing, the Chapter reflects a valid legislative concern for shareholder control over a fundamental event in the corporation's existence – the transformation of the corporation from a collection of dispersed shareholders to

one controlled by one dominant shareholder. If there is no shareholder vote and the dominant shareholder gains control of the board, the large group of remaining shareholders, "without its consent, is participating in a different enterprise as certainly as if there had been a merger with a third party." Brudney, *Equal Treatment of Shareholders*, 71 CAL. L. REV. 1072, 1122 (1983). The Control Share Chapter is thus squarely in the tradition of other State corporation statutes requiring shareholder votes on questions of fundamental corporate events such as mergers, dissolutions, sales of assets or changes in voting power of classes of shares – statutes that no one has seriously suggested are preempted by the Williams Act or other Federal securities statutes.[12]

The Seventh Circuit questioned at great length the substantive merits of the economic and policy decisions reflected in the Control Share Chapter – matters on which neither an academic nor a political consensus exists.[13] But the constitutional issue presented to the Seventh Circuit

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[12] The Control Share Chapter is also similar to legislation introduced in the 99th Congress by Senator Proxmire that would have required a two-thirds vote of a corporation's shareholders to approve a hostile takeover, while prohibiting the takeover bidder from voting its shares. *See* S. 706, 99th Cong., 1st Sess. (1985); 131 CONG. REC. S3243-48 (daily ed. Mar. 20, 1985) (statement of Sen. Proxmire). In the wake of recent revelations of insider trading in hostile takeovers, Senator Proxmire's proposal has received renewed attention. *See* Ingersoll, *supra* note 9.

Senator Proxmire's introduction of S. 706 in the last Congress underscores, of course, that neither the Williams Act nor other Federal securities laws deal with the concerns addressed by the Indiana legislature in the Control Share Chapter, and hence can scarcely preempt the Indiana statute.

[13] The substantive merits of the issues involved are extraordinarily complex, and particularly ill-suited to judicial (rather than legislative) resolution. Indeed, the Seventh Circuit's deci-

(Footnote continued on the following page)

(and to this Court) is *not* whether those decisions were wise or correct as a matter of policy or economics. Rather, the only relevant question as a matter of constitutional jurisprudence is whether, in our Federal system, those decisions were Indiana's to make.

The answer to that question is plain. One may debate whether the legislative history of the Williams Act im-

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13 *(Continued)*

sion, for all its focus on economics, ignores critical aspects of the economic forces that (in Professor Bebchuk's phrase) "distort" the choice faced by shareholders in responding to a hostile tender offer – particularly when the bidder attempts, as DCA did here, to obtain effective control by acquisition of less than all (and even less than a majority) of a corporation's shares. *See* Bebchuk, *supra* note 9, at 1717-33.

The Seventh Circuit's failure to analyze adequately even the economic impact of the Control Share Chapter is also illustrated by its apparent assumption that the Chapter is intended to protect incumbent management. (CTS App. at 25.) DCA makes the same assumption, asserting repeatedly that the Indiana statute is a "weapon" to defeat tender offers, "completely controlled by management." (*E.g.*, Motion To Affirm at 4-6, 7-8, 19-20.) Since the courts below decided the case without an evidentiary record, there is of course no evidentiary basis whatever for that claim. Moreover, it is impeached on the face of the statute itself, which (a) places the decision whether to accord voting rights to control shares in the hands of disinterested shareholders and *excludes* management; (b) requires a prompt shareholder vote at the instance of the acquiring person; (c) requires that notice of the meeting include the acquiring person's statement; and (d) contains nothing that prohibits the acquiror from communicating directly with the shareholders. *See* IND. CODE. § 23-1-42-7 & -8. If, as DCA maintains, tender offers in fact benefit all shareholders (*see* Motion To Affirm at 21-22), then one would expect disinterested shareholders to grant voting rights to the control shares and thus facilitate hostile takeovers. A statute that puts in the hands of the shareholders themselves the fate DCA claims will always benefit them is a curious "management entrenchment" device indeed.

plicitly preempts some State laws that also regulate disclosures to shareholders and the purchase and sale of securities. But in view of the narrow subjects regulated by the Williams Act, there is *no* basis for concluding that Congress made *any* political judgment to bar innovative State statutes that govern the voting power of shares in State-created corporations, or that deal with any other issue of corporation law not addressed by Williams Act regulation. To the contrary, Congress has traditionally left regulation of these internal corporate affairs to the State of incorporation. *Cort v. Ash*, 422 U.S. 66, 84 (1975). Indeed, the established validity of State authority to govern the internal affairs of corporations has led this Court to construe the Exchange Act narrowly so as *not* to "federalize . . . the law of corporations." *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977). *Accord, Schreiber v. Burlington Northern, Inc.*, 472 U.S. ___, 86 L. Ed. 2d 1 (1985) (§ 14(e) does not apply to alleged breaches of fiduciary duty by incumbent board of directors in tender offer contest).[14]

The decision below violates that principle, and its necessary implications highlight the error committed. The list of State laws that could be preempted under the Seventh Circuit's analysis is remarkably long. The Model Business Corporation Act – followed by many States – has long authorized directors to determine the relative voting rights of classes and series of shares, a power that obviously can be used to discourage a tender offer. *See* MODEL

[14] Indeed, in 1984 Congress rejected proposed legislation that would have restricted defensive tactics in takeover contests, H.R. 5693, 98th Cong., 2d Sess. (1984), in part because the bill would have intruded on State corporation law. *See Annual Review of Federal Securities Regulation*, 40 BUS. LAW. 997, 1019-21 (1985). *See also* H.R. Rep. No. 1028, 98th Cong., 2d Sess. 9-17 (1984) (noting that Congress must address proper relationship between State and Federal law in regulating takeovers), and note 12, *supra*.

BUS. CORP. ACT § 16 (1969); REV. MODEL BUS. CORP. ACT §§ 6.01(c), 6.02 (1984). State laws restricting voting to persons who have held shares in the corporation for a certain length of time, *e.g.*, IND. CODE §23-1-29-7 (record date may be 70 days before vote), could also be preempted. Statutes requiring shareholder votes on fundamental corporate events – *e.g.*, mergers, IND. CODE. § 23-1-40-3, sales of assets, IND. CODE. § 23-1-41-2, and dissolutions, IND. CODE § 23-1-45-1 – could certainly interfere with a tender offeror's desired takeover scheme and thus be preempted. State laws governing the timing of shareholder meetings, *e.g.*, IND. CODE §§ 23-1-29-1 *et seq.*, or the election of directors, *e.g.*, IND. CODE §§ 23-1-33-1 *et seq.*, may affect a tender offeror's ability to take control of a target corporation and thus also become constitutionally suspect.

The Seventh Circuit's suggestion that Williams Act preemption is analogous to Federal labor law preemption further illustrates this problem, and in fact underscores the basic flaw in the preemption analysis applied below. In the labor area, as the Seventh Circuit stated, Congress indeed established a "delicate balance between contending factions," leaving the forces of the marketplace to resolve contests and forbidding any State regulation tipping the regulatory balance in either direction. (*See* CTS App. at A22-23.) *Cf. Machinists v. Wisconsin Employment Relations Comm'n*, 427 U.S. 132, 150 (1976) (Congress meant to leave collective bargaining to the "free play of contending economic forces"). But Congress did so by enacting detailed, *comprehensive* legislation governing all aspects of the collective bargaining process; by establishing the supervisory role of the National Labor Relations Board over that process; and by authorizing the courts to develop a Federal common law of labor contracts to fill any remaining legal gaps, *see Textile Workers Union v. Lincoln Mills*, 353 U.S. 448, 456-57 (1957).

In the area of corporation law, however, Congress has done nothing that even approaches establishment of such a

comprehensive statutory, regulatory and judicial scheme. To the contrary, *State* law has always provided the comprehensive regulation, and thereby establishes whatever "balance" exists between contending forces in the corporate law field (including, *inter alia*, the "balance" on questions involving the voting rights of shares and other aspects of the legal relationships among shareholders). The Federal securities laws, by contrast, are only "incomplete and interstitial' in nature," *Kaminsky v. Abrams*, 281 F. Supp. 501, 505 (S.D.N.Y. 1968), addressed primarily to the purchase and sale of shares in interstate commerce.[15]

Hence, the flaw in the Seventh Circuit's labor law analogy is that Federal law could establish a "comprehensive balance of power" in tender offers only by Federalizing all aspects of corporation law that might affect that balance. As noted earlier, those aspects would include, in addition to the voting rights of control shares, a well-nigh limitless list of topics traditionally governed by State corporate statutes – such as the scheduling and voting methods for election of directors; the fiduciary standards applicable to defensive tactics in a tender offer; and the rights of a newly dominant shareholder to undertake a merger, dissolution or sale of assets to consolidate its position. Neither the Williams Act nor any other Federal statute even begins to address these issues.

[15] That Congress has established no comprehensive Federal scheme in the securities field at all analogous to that created by Federal labor legislation is underscored by the fact that the Williams Act governs only tender offers, *see* 15 U.S.C. § 78n(d)(1), and does not reach open market or privately negotiated purchases of securities – tactics recently employed in hostile takeover battles that can result in changes in corporate control with minimal Federal regulation. *See Hanson Trust PLC v. SCM Corp.*, 774 F.2d 47, 52-57 (2d Cir. 1985) (25% of company acquired in two hours in five private purchases and one open market purchase); Hertzberg & Rundle, *Campeau's Victory In Battle For Allied Signals Big Changes In Takeover Tactics*, Wall St. J., Nov. 4, 1986, at 2, col.3 (open market purchase of 48% of company in one day). The introduction of legislation in recent Congresses that *would* create greater Federal regulation of takeover battles also demonstrates that such regulation does not currently exist. *See* notes 12 & 14, *supra*.

Under the Seventh Circuit's analysis, however, all of these matters would, under the guise of Williams Act preemption, become subject to Federal judicial control. The Federal courts, unguided by any Federal statutory provisions, would have to establish the appropriate "balance" for all of these elements of corporation law, and then decide whether State statutes or State court decisions impermissibly "tipped" that balance – all by reference to some comprehensive standard of "neutrality" manufactured out of wholly judicial cloth.

The only apparent alternative to assigning these political decisions to Federal judges would be to hold that the Williams Act "froze," as of 1968, all aspects of the then-existing corporation laws of 50 States that might affect the "balance of power" in hostile takeovers. Since the Williams Act addresses only disclosures to shareholders and certain tender offer techniques, the statute itself plainly cannot supply the remainder of the regulatory "balance" that Congress (under the Seventh Circuit's reasoning) supposedly desired when it passed that statute. If that remaining "balance" is not to be created entirely by the Federal courts, then the only other apparent source is the 50-State pattern of corporation law as it existed in 1968 – a view under which virtually any post-1968 change in State corporation might be held to "upset the balance" and thus be preempted.

Both alternatives are plainly untenable. Congress intended neither to authorize the Federal courts to develop a general, Federal corporation law, nor to "freeze" State corporation law as of 1968. The Williams Act was instead a narrow statute intended to fill a small gap in Federal

securities regulation. In filling that gap, Congress may not *itself* have intended to tip whatever takeover "balance" then existed under each State's corporation laws. It gave no indication, however, that it intended the Williams Act to be the final and comprehensive word on takeovers, either by creating a Federal common law of corporations or by freezing State corporation law as of 1968.

Even assuming, then, that the "neutrality" observations in the Williams Act's legislative history could have any preemptive force, that force must be limited to the subjects actually regulated by the Williams Act – disclosures to shareholders and the purchase and sale of shares. That subject matter might at least provide a baseline by which courts could determine whether State statutes regulating the same subjects are "neutral" or not. Taken outside that limited context and applied to State corporation laws generally, however, the "neutrality" observations lack any substantive content to guide their application by the Federal judiciary. They become instead a roving mandate for the Federal courts to adjudicate whether any State corporation statute that may "affect" the desirability of tender offers is sufficiently "neutral" – adjudications that will likely be informed, as was the decision below, by little more than a given court's view of the economic and policy merits of tender offers. There is no meaningful, judicially manageable or constitutionally acceptable way to extend the "neutrality principle," as the Seventh Circuit did here, to State corporation statutes that do not govern disclosures to shareholders and the purchase and sale of shares.

II. THE CONTROL SHARE CHAPTER DOES NOT VIOLATE THE COMMERCE CLAUSE.

The Control Share Chapter does not discriminate in any way against interstate commerce or out-of-State residents. It applies only to Indiana corporations that also have other substantial ties to the State. Nor does the statute prohibit or regulate purchases of shares, whether in interstate commerce or otherwise. Instead, it regulates only the post-acquisition voting rights of control shares, however acquired, in the internal affairs of Indiana corporations.

Since the Chapter does not discriminate against interstate commerce and (as it applies only to Indiana corporations) poses no risk of overlapping and inconsistent State regulations, it plainly does not violate the Commerce Clause. By holding that it does, the Seventh Circuit impermissibly extended the reach of the "dormant" Commerce Clause into the States' traditional regulation of the internal affairs of the corporations they create.

Even if application of the "balancing test" articulated by this Court in *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), were proper in this case, it would not alter this conclusion. The Indiana statute serves the legitimate State purpose of protecting the interests of shareholders who may be adversely affected by a change in control of the corporation. Any indirect effects of the Chapter on interstate commerce are minor, especially since State law exclusively creates and defines the stock rights that are available for purchase in the first place. The Commerce Clause does not require the States to define shareholders' rights (or any other property rights) in any specific way, so long as the States do not discriminate against interstate commerce. The Seventh Circuit's holding to the contrary is unprecedented in Commerce Clause jurisprudence.

A. The Control Share Chapter Does Not Discriminate Against Interstate Commerce.

The first critical feature of the Control Share Chapter is that it does not discriminate against interstate commerce. The State's regulation of the voting rights of control shares does not turn on *any* feature of interstate commerce. The statute applies whether the Indiana corporation's control shares are acquired in intrastate or interstate

commerce, and whether through a tender offer, private or open market purchases or otherwise. Likewise, it applies regardless of the residences of the buyer and seller.

The Chapter therefore easily passes the most basic test of Commerce Clause analysis. This Court accords "special deference" to State laws that do not discriminate against interstate commerce, based on the sound assumption that where a law's "burden usually falls on local economic interests as well as other States' economic interests, [this ensures] that a State's own political processes will serve as a check against unduly burdensome regulations." *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 675 (1981) (plurality opinion). *Accord, Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 125-26 (1978) (no discrimination even where burden fell only on out-of-State businesses); *Huron Portland Cement Co. v. Detroit*, 362 U.S. 440, 448 (1960) (no discrimination).[16]

B. The Control Share Chapter Applies Only To Indiana Corporations And Poses No Risk Of Multiple And Inconsistent Burdens.

The second critical feature of the Control Share Chapter for Commerce Clause purposes is that it applies only to Indiana corporations with additional ties to the State. Therefore, the statute poses no risk of subjecting the corporation or a tender offeror to cumulative, multiple and inconsistent State regulations. In addition to discrimination, the presence or absence of this risk of multiple burdens plays the other major role in Commerce Clause jurisprudence. In *MITE*, for example, the Illinois statute

[16] The *Kassel* plurality concluded that this traditional deference was weakened where the State also created several exemptions that clearly reduced the burden of the regulations on its own residents. 450 U.S. at 676-78. The Indiana Control Share Chapter contains no such discriminatory exemptions.

at issue prohibited certain stock purchases pursuant to tender offers, and was not limited to corporations chartered under Illinois law. Hence, Justice White's opinion noted that "if Illinois may impose such regulations, so may other States; and interstate commerce in securities transactions generated by tender offers would be thoroughly stifled." 457 U.S. at 642.

Huron Cement made the same point: "State regulation, based on the police power, which does not discriminate against interstate commerce *or operate to disrupt its required uniformity*, may constitutionally stand." 362 U.S. at 448 (emphasis added). *See also Southern Pacific Co. v. Arizona*, 325 U.S. 761, 774 (1945) (striking down State limit on train length in view of "confusion and difficulty" resulting from conflicting State regulations); *Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520, 529-30 (1959) (striking down one of conflicting State regulations on the shape of truck mud-flaps). In this case, there is obviously no need for national uniformity in shareholder voting rights (unlike, for example, railroad or trucking regulation). Furthermore, there is no risk of overlapping and inconsistent State regulation because the law of one State – and one State only –*must* define shareholder voting rights.

The absence of both discrimination against interstate commerce and any risk of overlapping and inconsistent State regulations should dispose of the Commerce Clause issue here. *See Huron Cement*, 362 U.S. at 448. Despite various formulations of the test, this Court has *never* struck down on Commerce Clause grounds State legislation that did not exhibit at least one of these features.[17]

[17] As one variant of the "multiple burden" aspect of Commerce Clause analysis , the Court has stricken State laws that "directly regulate" interstate commerce – such as the Illinois statute in

(Footnote continued on the following page)

C. The Control Share Chapter Serves Legitimate State Interests In Protecting Non-Dominant Shareholders In Indiana Corporations.

In *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970), this Court articulated a balancing test for "evenhanded" regulations "affecting" interstate commerce:

> Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits.

In *Pike* itself, however, this "balancing test" was not applied, since that case involved a statute that discriminated on its face against interstate commerce (requiring produce grown in the State to be packaged there as well, *see* 397 U.S. at 145). Since *Pike*, this Court has applied this "balancing test" to invalidate State laws only where the threat of multiple and inconsistent burdens on interstate commerce existed. *E.g., Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 441-46 (1978). *See generally* Regan, *The Supreme Court And State Protectionism: Making Sense Of The Dormant Commerce Clause,* 84 MICH. L. REV. 1091 (1986). Since the Indiana Control Share Chapter, which applies only to Indiana corporations, presents no threat whatever of multiple and inconsistent State regulations, CTS submits at the outset that the *Pike*

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MITE, which forbade the purchase and sale of shares nationwide, including transactions between wholly out-of-State parties. 457 U.S. at 641-42. *See also Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. ___, 90 L. Ed. 2d 552, 561-63 (1986). Indiana's Control Share Chapter, which does not regulate purchase and sale transactions at all, imposes no such restriction.

"balancing test" is wholly inapplicable here.[18]

Even assuming *arguendo*, however, that the *Pike* test applies at all in this case, the balance of interests is heavily in favor of the State statute. The Control Share Chapter protects non-dominant shareholders in Indiana corporations whose interests may be adversely affected by a change in control of the corporation. By permitting these shareholders to decide whether voting control of the corporation should change hands through acquisition of the

[18] There are severe conceptual difficulties in applying the *Pike* "balancing test" in cases where there is no threat of multiple and inconsistent State burdens upon interstate commerce. The "values" or "interests" as between State law and interstate commerce are simply incommensurate, and a court attempting to strike the "balance" would be placed squarely in the proverbial (and plainly legislative) role of weighing "apples against oranges" – something this Court has consistently said it will not do. *See, e.g., Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 670 (1981) (opinion of Powell, J., joined by White, Blackmun and Stevens, JJ.) ("if safety concerns are not illusory, the Court will not second-guess legislative judgment about their importance in comparison with related burdens on interstate commerce"); *id.* at 691 (Rehnquist, J., joined by Burger, C.J., and Stewart, J., dissenting) ("the Court does not directly compare safety benefits to commerce costs and strike down the legislation if the latter can be said in some vague sense to 'outweigh' the former. Such an approach would . . . arrogate to this Court the functions of forming public policy, functions which, in the absence of congressional action, were left by the Framers of the Constitution to state legislatures"); *Raymond Motor Transportation, Inc. v. Rice*, 434 U.S. 429, 450 (1978) (Blackmun, J., joined by Burger, C.J., and Brennan and Rehnquist, JJ., concurring) ("the Court does not engage in a balance of policies; it does not make a legislative choice"). Moreover, as this Court held only last term, even a State law that *discriminates* against interstate commerce will still survive constitutional scrutiny if it serves legitimate (*i.e.*, non-protectionist) purposes that

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control shares by a single dominant person, the statute serves the legitimate State purpose of protecting their interests and promoting shareholder control over fundamental changes in the corporation. As discussed at greater length earlier in addressing the Supremacy Clause issue, minority or dispersed shareholders are vulnerable to exploitation by a dominant shareholder who may run the corporation for its own benefit.

Indiana, like its sister States, has commonly required shareholder approval of fundamental changes in corporate affairs, a tradition continued by the new Indiana Business corporation Law. *See, e.g.,* IND. CODE §§ 23-1-38-3 (amendments to articles of incorporation); 23-1-40-3 (mergers and share exchanges); 23-1-41-2 (dispositions of substantial assets); and 23-1-45-2 (dissolutions). The Control Share Chapter's requirement of a disinterested shareholder vote reflects the Indiana legislature's conclusion that a single dominant shareholder's acquisition of a substantial block of shares is also a fundamental change for the corporation, and should also be subject to shareholder approval as to the voting rights of that block of shares. That legislative judgment should not be second-guessed by the courts when the statute neither discriminates against interstate commerce nor regulates any

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18 *(Continued)*

"could not be served as well by available nondiscriminatory means." *Maine v. Taylor*, 477 U.S. ___, 91 L. Ed. 2d 110, 121 (1986). There is no "second tier" balancing test by which the Court also "weighs" the State interest served by the discriminatory State law against the burden on interstate commerce. *See id.* at 121-129. Hence, to use a "balancing" test in cases that involve no threat of multiple and inconsistent burdens would, perversely, leave the courts freer to act as legislatures and invalidate State policy judgments with which they disagree – as happened here in the courts below – than in cases of *discriminatory* State laws that implicate the core values of the Commerce Clause.

interstate transaction in the first place.

The Seventh Circuit dismissed Indiana's interests as "trivial or even negative," saying that "Indiana has no interest in protecting residents of Connecticut from being stampeded to tender their shares to [DCA] at $43." (CTS App. at A25 (citing *MITE*).) That simplistic analysis elides both the far different context of *MITE* and the State's actual interests in the case at bar. Unlike the Illinois statute in *MITE*, the Indiana statute at issue here has utterly no effect on any shareholder's ability to *sell* his shares. Rather, the Control Share Chapter protects shareholders of Indiana corporations – both resident and nonresident and including those who decide *not* to tender or otherwise dispose of their shares – in the event of a potentially adverse change in voting control of the corporation.

The Seventh Circuit's reasoning also misreads Justice White's opinion in *MITE*, apparently relying on the following passage:

> While protecting local investors is plainly a legitimate state objective, the State has no legitimate interest in protecting nonresident shareholders. Insofar as the Illinois law burdens out-of-state transactions, there is nothing to be weighed in the balance to sustain the law.

457 U.S. at 644. That statement in *MITE* dealt with an Illinois statute that was *not* limited to Illinois corporations and that *did* regulate purchases and sales of shares between wholly out-of-State sellers and buyers. Indiana, however, obviously has a legitimate interest in protecting *all* shareholders of Indiana corporations in their relationships *inter sese,* including voting rights. More generally, the State is entitled to take steps to protect the investments of nonresidents as well as residents. That is a legitimate interest that necessarily inheres, in one form or another,

in the corporation code of every State.[19]

D. Any "Effects" Of The Control Share Chapter On Interstate Commerce Do Not Burden Such Commerce And Do Not Rise To Constitutional Significance.

The other factor to be weighed in the *Pike* "balancing test" is a State statute's burden on interstate commerce. Hence (assuming again that the *Pike* test applies here at all), the Control Share Chapter would violate the Commerce Clause only if it imposed a burden on interstate commerce that is "clearly excessive" in relation to the State's interest in protecting non-dominant shareholders. The "burdens" found by the Seventh Circuit, far from constituting the "excessive" interference with interstate commerce required by *Pike*, reflect fundamental misunderstandings both of State corporation law and of this Court's Commerce Clause jurisprudence.

The Seventh Circuit apparently recognized that the Control Share Chapter does not prohibit interstate commerce in equity securities. Rather, the heart of the Seventh Circuit's Commerce Clause analysis here was its judgment (based on *no* evidence) that the Indiana statute impedes a "commerce in corporate control" that the Seventh Circuit deemed "important." (CTS App. at

[19] So long as a State allows out-of-State residents to own shares in its domestic corporations (as it constitutionally must), then any State corporation law regulating voting rights or any other internal corporate relationship will necessarily have extraterritorial effects. To suggest that Indiana law should *discriminate* between voting rights of resident and non-resident shareholders would create (rather than avoid) constitutional problems. *See Supreme Court of New Hampshire v. Piper,* 470 U.S. 274, 280 (1985)(Privileges and Immunities Clause " 'guarantees to citizens of State A [the privilege] of doing business in State B on terms of substantial equality with the citizens of that State," ' *quoting Toomer v. Witsell,* 334 U.S. 385, 396 (1948)).

A26.)[20] Specifically, the Seventh Circuit reasoned that the efficiency with which a corporation's assets are employed "depends on the market for corporate control – an interstate, indeed international, market that the State of Indiana is not authorized to opt out of, as in effect it has done in this statute." *Id.* Of course, this *ipse dixit* is simply wrong. Nothing in the Commerce Clause requires the States to create corporations at all, much less – as the Seventh Circuit held – to define the rights of shareholders so as to tie the voting rights of a share inextricably to the equity interest in the corporation's profits and property represented by a share.[21]

[20] In addition to the lack of any evidence supporting the Seventh Circuit's speculations about impact upon "commerce for corporate control," there is also no evidence to show (and no basis whatever to assume) that the Control Share Chapter will cause any reduction in the total "amount" of commerce, interstate or intrastate, in the equity securities of covered Indiana corporations. At most, there may be come *shift* in the persons doing the trading – *i.e.,* from tender offerors to other investors – an effect that is absolutely immaterial for Commerce Clause purposes. *See Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, 127 (1978) ("interstate commerce is not subjected to an impermissible burden simply because an otherwise valid regulation causes some business to shift from one interstate supplier to another" ; "the Clause protects the interstate market, not particular interstate firms").

[21] This conclusion, implicit in the Seventh Circuit's opinion, was stated explicitly by the District Court: "Voting rights, after all, are an integral part of the ownership interest purchased along with a stock certificate." (CTS App. at A79.) "The value of the shares in control acquisitions is inseparable from their voting power." (CTS App. at A114.)

This stress on the importance of voting rights is more than a little ironic, since State law is the *source* of all such rights. The "one share, one vote" rule, for example, is neither universal nor constitutionally required. *See Providence & Worcester Co. v. Baker,* 378 A.2d 121, 123 (Del. 1977) (at common law each shareholder had one vote regardless of number of shares owned). Nothing in the Constitution would prohibit a State frcm

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The Seventh Circuit made two fundamental errors. First, Judge Posner's opinion mistakenly equates economic efficiency with constitutionality. But this Court's decision in *Exxon* makes clear that a State may impose "inefficient" regulations on commerce to further other goals, such as fairness to all shareholders. In *Exxon,* the fact that a State law altered "the natural functioning of the interstate market" was unimportant because the Commerce Clause does not protect "the particular structure or methods of operation" in a market. 437 U.S. at 127. Thus, Maryland was entitled to protect independent service station operators even if it was not "economically efficient" to do so.

The Seventh Circuit's concern about the efficient use of corporate assets here – like the plaintiffs' argument in *Exxon* – "relates to the wisdom of the statute, not to its burden on commerce." 437 U.S. at 128. The efficiency argument should therefore be addressed to the Indiana legislature, not to the Federal courts. Indeed, the Seventh Circuit's entire "interstate market for corporate control" theory is but a thinly disguised variation on the "novel suggestion," rejected in *Exxon,* that "because the economic market for petroleum products is nationwide, no State has the power to regulate the retail marketing of gas." 437 U.S. at 128.

Equally important, Judge Posner's reasoning fails to realize that the "market for corporate control" is a market *created only by State law defining property rights and ownership interests.* The "market" exists at all only because Indiana and other States (acting under no "Commerce Clause" or other constitutional compulsion) have enacted laws that create corporations in the first

21 *(Continued)*

adopting a "one shareholder, one vote" rule today, even though such a rule would make it difficult – if not impossible – for a hostile takeover bidder to acquire control of that State's corporations.

place, and then permit them to issue equity securities that may then in turn be bought and sold. As Chief Justice Marshall explained long ago:

> A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence.

Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819). *State* law defines the terms of the contract among the corporation, its shareholders and the State, and thereby (as is true of all State-created property interests) *defines* any interest that is available for sale, whether in interstate commerce or otherwise.[22]

Moreover, nothing in this Court's Commerce Clause decisions even suggests that the States may not, in exchange for the privileges of the corporate franchise, impose conditions on those privileges – including limits on the transfer of voting power that do not discriminate against interstate commerce. Indeed, this Court has upheld similar limits. For example, in *Louisville & Nashville R.R v. Kentucky,* 161 U.S. 677 (1896), this Court upheld

[22] Ironically, the same panel of the Seventh Circuit that decided the case now before this Court recognized, in deciding a later appeal involving CTS's second shareholder rights plan, that the Commerce Clause does not invalidate contractual relationships among shareholders governed by State corporation law. Thus, in rejecting as "frivolous" DCA's argument that Indiana law violated the Commerce Clause by allowing defensive tactics by the boards of directors of its domestic corporations, the panel stated: "The commerce clause does not require states to outlaw private contracts that may impede interstate commerce." *Dynamics Corp. of America v. CTS Corp.,* No. 86-1888, slip op. at 23 (7th Cir. Nov. 3, 1986). The Control Share Chapter itself, however, involves nothing more than such a "private contract" among the shareholders with respect to voting rights – particularly since Indiana corporations are given the choice of "opting-out" of the Control Share Chapter. *See* IND. CODE § 23-1-42-5.

against a Commerce Clause challenge a State's prohibition on a State-chartered railroad's purchase of competing railroads:

> As the power to purchase, then, is derivable from the state, *the state may accompany it with such limitations as it may choose to impose.* It results, then, from the argument of the appellant, that if there be any interference with interstate commerce *it is in imposing limitations upon the exercise of a right which did not previously exist*; and hence, if the state permits such purchase or consolidation, it is bound to extend the authority to every possible case, or expose itself to the charge of interfering with commerce. *This proposition is obviously untenable.*

161 U.S. at 702-03 (emphasis added).[23]

The lesson of these cases is clear: Absent discrimination against interstate commerce, nothing in the Commerce Clause requires the States to define corporate property rights and ownership interests in particular ways. More generally, the fact that alternative legal definitions of property might lead to a larger "interstate market" in the property as redefined does not, even if proven, estab-

[23] Similarly, this Court has often recognized that the law of the State of incorporation defines and creates corporate property rights, and therefore must govern relationships among shareholders and the corporation. For example, in *Modern Woodmen of America v. Mixer,* 267 U.S. 544, 551 (1925), the Court held that the Full Faith and Credit Clause required the forum State court to apply the law of the State of incorporation, and not its own, to determine the rights of a shareholder. Accordingly, the *Modern Woodmen* Court upheld a limitation on a shareholder's rights imposed by the law of the State of incorporation: "The act of becoming a member is something more than a contract, it is entering into a complex and abiding relation, and as marriage looks to domicil, membership looks to and must be governed by the law of the State granting the incorporation." *Id. Accord, e.g., Royal Arcanum v. Green,* 237 U.S. 531, 546 (1915); *Head & Amory v. Providence Ins. Co.,* 6 U.S. (2 Cranch) 127, 167 (1804).

lish a Commerce Clause violation. For example, it could not credibly be argued that a State law permitting private ownership of handguns but forbidding their sale violates the Commerce Clause, even though such a statute would reduce the "amount" of interstate (as well as intrastate) commerce in that property.

DCA's Commerce Clause contentions do nothing to alter this conclusion. The essence of DCA's argument is that the Control Share Chapter violates the Commerce Clause because DCA is an out-of-State corporation and its tender offer involved interstate commerce. Neither fact, however, raises any constitutional issue with respect to a State statute that *also* applies to any *in*-State takeover bidder, and *also* applies to a tender offer (or other acquisition) involving wholly *intra*state commerce. In short, DCA seeks not the absence of discrimination that the Commerce Clause ensures, but rather claims some right to special treatment simply because its takeover bid involved interstate commerce. Justice Holmes long ago rejected that argument for the Court: "A man cannot acquire a right to property by his desire to use it in commerce among the States. Neither can he enlarge his otherwise limited and qualified right to the same end." *Hudson County Water Co. v. McCarter,* 209 U.S. 349, 357 (1908). Likewise, while the Commerce Clause may prohibit Indiana from discriminating against DCA because it is an out-of-State corporation, it does not entitle DCA to special privileges arising from its non-resident status.

The Seventh Circuit's various comments about the wisdom of the economic policy judgments reflected in the Control Share Chapter are also of no constitutional moment under the Commerce Clause. For example, the Seventh Circuit characterized the belief that "hostile takeovers are bad" as "benighted," while describing "commerce in corporate control" as "important." (CTS App. at A22, A26.) Both comments reflect a profound misunderstanding of the Commerce Clause and the role of the Federal courts in applying it. There may indeed cur-

rently exist, as a practical matter, a familiar market in "corporate control." Indiana has simply chosen, however, as a matter of its generic corporation law, to give shareholders of its domestic corporations new rights vis-a-vis potentially dominant new shareholders. Whether the Seventh Circuit found this new type of law unsettling, unwise or even "benighted," it overlooked that:

> Some . . . laws embody convictions which judges are likely to share. Some may not. But a Constitution is not intended to embody a particular economic theory, whether of paternalism and the organic relation of the citizen to the state or of *laissez faire*. It is made for people of fundamentally differing views, and the accident of our finding certain opinions natural and familiar, or novel, and even shocking, ought not to conclude our judgment upon the question whether statutes embodying them conflict with the Constitution of the United States.

Lochner v. New York, 198 U.S. 45, 75-76 (1905) (Holmes, J., dissenting). And, as noted earlier, this Court's decision in *Exxon* makes clear that the Commerce Clause does not require the States to continue to maintain economically "efficient" markets, even where interstate commerce is in some sense "affected." *See* L. TRIBE, AMERICAN CONSTITUTIONAL LAW 25 (Supp. 1979) (discussing *Exxon*); *New State Ice Co. v. Liebmann,* 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) ("[i]t is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country").

In fact, the Seventh Circuit's comments about "benighted" views and "important" commerce in corporate control reflect but one side of a long-standing and substantial debate over the value of the extensive hostile takeover activity in the American economy – a debate intensified in just the last few weeks by renewed attention focused on the role of the arbitrage community. The very existence of that debate, however, supports Indiana's right to

undertake the economic experiment of the Control Share Chapter. If the Seventh Circuit's economic analysis were correct, one might reasonably expect the market price for shares in Indiana corporations to drop. If that should occur – and whether it will is highly questionable – it would harm only Indiana and thus raise no Commerce Clause issue. *See Raymond Motor Transportation, Inc. v. Rice,* 434 U.S. 429, 444 n.18 (1978). Indeed, Indiana's allegedly "benighted" experiment, if it should prove to be such, may save the rest of the States or Congress from making the same mistake on a much larger and costlier scale. That is precisely the view of economic Federalism that Justice Brandeis praised in *New State Ice.*[24]

The Seventh Circuit's disregard of these fundamental principles of Federalism – and its substitution of its own economic policy analysis for Commerce Clause

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[24] Equally insignificant for Commerce Clause purposes is the claim – implied by the Seventh Circuit (CTS App. at 25) and overtly argued by DCA (Motion To Affirm at 16, 18) – that the Indiana statute "protects" incumbent management of Indiana corporations. Even if that were the purpose or effect of the statute – a debatable proposition on which there is no record evidence, *see* note 13, *supra* – it is *not* the sort of "economic protectionism" *between States* that the Commerce Clause forbids, any more than was the "economic protectionism" of independent service station operators upheld in *Exxon*. Absent "protectionism" directed at its sister States, Indiana is free to make the legislative judgment that leaving corporations wide open to corporate raiders leads to undesirable economic results – with incumbent management focusing only upon short-term results and the current market price of the corporation's stock, rather than undertaking economically rational risks and investments that pay off only in the longer term. *See, e.g.,* Lowenstein, *Pruning Deadwood In Hostile Takeovers: A Proposal For Legislation,* 83 COLUM L. REV. 249, 291-306 (1983). Even if the Commerce Clause *did* impose any "economic inefficiency" constraint on State legislative action (and it does not), it certainly does not impose a *particular school* of economic thought on the States of this Nation.

jurisprudence – are highlighted by its twin statements that the fact "that the mode of [State] regulation involves jiggering with voting rights cannot take it outside the scope of [Federal] judicial review," and that any other conclusion would invite "facile evasions" of the Commerce Clause. (CTS App. at A27). Neither statement is correct.

Both the Constitution in general and the Commerce Clause in particular are precisely concerned with which "mode[s]" of regulation are the province of the Federal Government and which are the province of the States. The proper focus of constitutional inquiry is where the Constitution places the power to act – an inquiry that does not turn on whether regulation will or will not yield a given economic result in a particular case. *Cf. Synar v. United States,* 626 F. Supp. 1374, 1403 (D.D.C.) ("the balance of separated powers established by the Constitution consists precisely of a series of technical provisions that are more important to liberty than superficially appears, and whose observance cannot be approved or rejected by the courts as the times seem to require"), *aff'd sub nom. Bowsher v. Synar,* 478 U.S. ___, 92 L. Ed. 2d 583 (1986). A State statute of the kind at issue here – regulating (as the States have traditionally and exclusively done) the voting power of shares in corporations created by that State – is not invalid simply because one of its effects may be to make the purchase of such shares less attractive as an *economic* proposition for a prospective acquirer. Whether the Commerce Clause is "honored" or "evaded" depends not on whether a given economic outcome is reached, but rather on whether the Federal Government and the States are acting within their respective spheres of constitutional authority.

Moreover, the logic of the Seventh Circuit's contrary Commerce Clause reasoning points (like its preemption analysis) inexorably in one direction: Any aspect of State corporation law that may make it harder to take over voting control of a domestic corporation violates the Commerce Clause. While the Seventh Circuit "assume[d]

without having to decide that Indiana has a broad latitude in regulating [the internal affairs of its corporations], even when the consequence may be to make it harder to take over an Indiana corporation" (CTS App. at A27), its reasoning in fact has no stopping point. It reaches any aspect of State corporation law that may discourage a takeover: The Seventh Circuit articulated no logical distinction between such laws, and none exists. If a State may not "jigger with voting rights," there is no reason why it may "jigger" with the scheduling and voting methods for electing directors, fiduciary standards applicable to takeover defenses, restrictions on freeze-out or back-end mergers that may injure minority shareholders, or any other aspect of State corporation law that may annoy a given tender offeror.

But the Commerce Clause does not reach so far. Because the Control Share Chapter neither discriminates against interstate commerce nor creates a threat of multiple and inconsistent burdens, Indiana remains free to try this economic experiment in protecting the interests of non-dominant shareholders in the corporations it creates.

CONCLUSION

In view of the wide-spread policy debate over the desirability of hostile corporate takeovers and the prospect of unlimited Federal intrusion into State corporation law, the appropriate balancing of State and Federal regulation should be left to the political judgments of State legislatures and the Congress. To date, the Congress has involved itself in tender offer regulation only to the limited extent of the Williams Act, which does not even begin to address the subjects covered by the Control Share Chapter. Unless and until Congress speaks to the contrary, Indiana should be permitted to proceed with an economic experiment that does not conflict with the Williams Act, and neither discriminates against interstate commerce nor extends beyond its own corporations.

This Court should therefore reverse the judgment below.

December 3, 1986.

Respectfully submitted,

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Nos. 86-71, 86-97

In The

Supreme Court of the United States

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

STATE OF INDIANA,

Intervenor-Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

On Appeal From The United States Court Of Appeals For The Seventh Circuit

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BRIEF FOR APPELLEE DYNAMICS CORPORATION OF AMERICA

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QUESTION PRESENTED

Whether the Control Share Chapter of the Indiana Business Corporation Law (the "Chapter") is unconstitutional where:

1. The Chapter (a) has a protectionist purpose, (b) directly regulates interstate commerce between nonresident parties, (c) has discriminatory effects on interstate commerce and (d) burdens interstate commerce in a manner that far outweighs any local benefits; and

2. The Chapter conflicts with (a) the Williams Act's market method of investor protection by subjecting a shareholder's decision to sell its shares to the prior approval of management and at least two shareholder groups and (b) the policy of neutrality between management and tender offerors upon which the investor protections of the Williams Act rest.

PARTIES TO PROCEEDINGS BELOW

Seventh Circuit No. 86-1601 involved the constitutional questions presented by this appeal. The parties were: Dynamics Corporation of America ("DCA"), as plaintiff-appellee; CTS Corporation ("CTS"), Robert D. Hostetler, Gary B. Erekson, and Joseph DiGirolamo (officers and/or directors of CTS), as defendants-appellants; and the State of Indiana ("Indiana"), as intervenor-appellant.

Seventh Circuit No. 86-1608 involved the same action in the District Court, was consolidated with No. 86-1601, but did not involve the constitutional questions presented by the present appeal. The parties were: DCA, Andrew Lozyniak, Edward J. Mooney, Henry V. Kensing, Patrick J. Dorme, Frank A. Gunter, Curtis T. Roff, Saul Sperber, Joseph P. Walker and Harold Cohan (officers and/or directors of DCA) as plaintiffs-appellees; and CTS, Robert D. Hostetler, Gary B. Erekson, Joseph DiGirolamo, George F. Sommer, Gerald H. Frieling, Jr., Don J. Kacek, Ted Ross and Richard M. Ringoen (officers and/or directors of CTS) as defendants-appellants.

Rule 28.1 Listing. Appellee DCA has no parent corporation, non-wholly owned subsidiaries, or affiliates.

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CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

This case involves the following constitutional provisions and statutes:

1. Supremacy Clause, U.S. CONST. art. VI, cl. 2.
2. Commerce Clause, U.S. CONST. art. I, § 8, cl. 3.
3. Williams Act Amendments to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78l(i) 78m(d)-(e) 78n(d)-(f) (1982 & Supp. III 1985).
4. Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE §§ 23-1-42-1 to 11 (1986).

COUNTER-STATEMENT OF THE CASE

In their statements of the case, appellants[1] argue that the Chapter is merely a voting provision which does not "restrict," "govern" or "regulate" interstate tender offers or the interstate purchase and sale of securities. (CTS Br. at 3-4, Ind. Br. at 10-11.) Such assertions, however, ignore the Chapter's provisions and the facts of this case.

A. The Chapter Regulates Interstate Tender Offers And Securities Transactions

The Chapter is part of the revised Indiana Business Corporation Law ("Business Corporation Law"), IND. CODE §§ 23-1-17-1 to 23-1-54-2 (1986).[2] It removes existing shareholder voting rights from so-called "control shares." IND. CODE § 23-1-42-1. The Chapter defines "control shares" as the block of shares of an Indiana corporation that when purchased will put an "acquiring person" over certain share ownership thresholds: 20%, 33.3% and 51%. IND. CODE § 23-1-42-1. It applies to a variety of "control share acquisitions," including interstate tender offers which cross any of the ownership thresholds. IND. CODE § 23-1-42-1. The Chapter governs tender offers even if 90% of the corporation's shareholders, its principal place of business, its principal office and the tender offeror are located outside Indiana. IND. CODE § 23-1-42-4.

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[1] DCA respectfully requests the Court's indulgence when it refers to "appellants" rather than the more unwieldy formulation "CTS and Indiana." *See* Fed. R. App. P. 28(d). Their arguments are substantially the same.

[2] The Chapter does not contain a statement of purpose and no official legislative history of the Business Corporation Law has been published. Section 23-1-17-5 of the Business Corporation Law permits a General Corporation Law Study Commission to publish official comments on the Chapter. No such comments have been published as of January, 1987. If later published, such comments should be given little weight by this Court because they will have been drafted after DCA challenged the Chapter.

The Chapter applies to all Indiana corporations that are "issuing public corporations."[3] IND. CODE § 23-1-42-5. At the same time it establishes procedures by which incumbent management may decide whether and when to invoke its provisions. The Chapter empowers incumbent management to opt out of (or back into) the Chapter without shareholder approval. IND. CODE § 23-1-42-5. *See also* IND. CODE § 23-1-22-4(c)(3) (permitting Indiana corporations to adopt defensive measures against changes in corporate control without shareholder approval). It imposes no limits on managerial discretion.

Once it is triggered, the Chapter removes the voting rights from all shares tendered. The statute applies regardless of the nature of the tender offer or the intentions of the tender offeror. It applies regardless of the performance of incumbent management or the potential benefits of the acquisition to shareholders, the corporation or Indiana citizens. The tender offeror can only recover its voting rights pursuant to a statutory procedure administered by management and "only to the extent granted by resolution approved by the shareholders . . . ." IND. CODE § 23-1-42-9(a).[4] At a minimum, a majority of (1) all shareholders *and* (2) all shareholders "excluding all interested shares" must

[3] The Chapter as part of the Business Corporation Law becomes generally applicable on August 1, 1987. IND. CODE § 23-1-17-3(b). Indiana corporations were permitted to opt into the Business Corporation Law after April 1, 1986. IND. CODE § 23-1-17-3(b)(1)-(2). CTS was the first Indiana corporation to adopt the Business Corporation Law. (R. 55, Exh. A.)

[4] Thus, the Chapter allows management to propose that the acquiring person be granted restricted voting rights. Such restricted voting rights might, for example, prohibit the acquiring person from participating in the selection of the company's board of directors. *See* IND. CODE § 23-1-42-9(b)(2). Gaining limited voting rights would be a Pyrrhic victory for the acquiring person because the Chapter permits management to redeem shares not given full voting rights. IND. CODE § 23-1-42-10(b).

approve a resolution reenfranchising the "control shares" with some or all of the voting rights. IND. CODE § 23-1-42-9(b).[5] Shareholders are disqualified from voting on the voting rights resolution as "disinterested" persons if the tender offeror votes their proxies. IND. CODE § 23-1-42-3(1).

The tender offeror can request a special shareholders meeting on the voting rights issue. IND. CODE § 23-1-42-7(a). The request is not a vehicle for "prompt" shareholder resolution of that issue. (CTS Br. at 4.) Although federal law permits tender offerors to purchase tendered shares 20 business days (*circa* 28 calendar days) after making a tender offer, 17 C.F.R. § 240.14e-1a (1986), the Chapter allows management to delay the meeting for 50 days, IND. CODE § 23-1-42-7(b). In practice, resolution of the voting rights issue will take longer than 50 days, considering the time it will take to count the shareholder ballots and to conclude any litigation arising out of the special shareholders meeting, proxy solicitations and ballot counting process.[6] If this delay is only 10 days beyond the 50 day period, the tendering shareholders will regain their withdrawal rights under the Williams Act,

[5] In control share transactions that implicate § 23-1-38-4(a) of the Indiana Business Corporation Law by, for example, causing the issuance of a new class of stock, more than two voting groups must approve the voting rights resolution. *See* IND. CODE § 23-1-42-9(b)(1). Appellants' self-serving interpretation of § 23-1-42-9(b) is contrary to its plain language and the interpretations of the District Court, CTS App. 38-39, the Seventh Circuit, CTS App. at 20, and other courts that have considered similar voting requirements. *See, e.g., Fleet Aerospace Corp. v. Holderman*, 637 F. Supp. 742, 750-53 (S. D. Ohio), *aff'd*, 796 F.2d 135 (6th Cir.) *appeal docketed*, No. 86-344 (U.S. Sept. 2, 1986); *Icahn v. Blunt*, 612 F. Supp. 1400, 1406-1407 (W.D. Mo. 1985).

[6] There is an inevitable delay in counting the votes after a shareholders meeting. For example, in this case it took 14 days

(Footnote continued on the following page)

15 U.S.C. § 78n(d)(5). The exercise of these withdrawal rights willterminate a tender offer.[7]

To obtain a special shareholders meeting, the tender offeror must file an "acquiring person statement" and give an undertaking to pay the corporation's expenses of holding a special shareholders meeting. IND. CODE § 23-1-42-7(a).[8] The information to be supplied in the acquiring person statement is duplicative of that which tender offerors must supply to the corporation and its shareholders under the Williams Act, 15 U.S.C. § 78m(d)(1). The Chapter does not require the tender offeror to disclose any additional information which may help shareholders resolve the voting rights issue. IND. CODE § 23-1-42-8(b).

The Chapter allows management to redeem any purchased shares not accorded full voting rights "at the fair value thereof pursuant to the procedures adopted by the corporation." IND. CODE § 23-1-42-10(a)-(b). The Chapter does not define "fair value" for purposes of the corporation's redemption of the tender offeror's shares. It may, however, require tender offerors to pay dissenting shareholders for their shares at a "fair value" above market price.

6 *(Continued)*

to tally the votes cast at the 1986 CTS Annual Meeting. *See Dynamics Corp. of America v. CTS Corp.*, 643 F. Supp. 215, 216-217 (N.D. Ill. 1986). DCA challenged the election results. It took the District Court approximately three weeks to rule on DCA's request for a preliminary injunction in connection with its challenge.

[7] If, upon the expiration of the 60 day period, the tender offeror makes a revised offer, then management could require the tender offeror to file a revised acquiring person statement, and the 50 day period for a shareholder vote would begin running anew.

[8] It is unclear under the Chapter whether the acquiring person is responsible for the corporation's litigation expenses arising out of the special shareholders meeting, which expenses could be substantial.

IND. CODE § 23-1-42-11(b)-(c). The Chapter also regulates those tender offerors who do not file an acquiring person statement. It permits management to delay a vote on a voting rights resolution until the next annual meeting. IND. CODE § 23-1-42-7(c).[9] The Chapter also empowers management to redeem the shares tendered to the non-filing tender offeror 60 days after announcing the tender offer. IND. CODE § 23-1-42-10(a).

B. This Case Illustrates The Chapter's Regulatory Impact On Interstate Tender Offers

CTS is an Indiana corporation and DCA is a New York corporation headquartered in Connecticut. (CTS App. at 5.) Both companies are publicly owned and their stock is traded on the New York Stock Exchange. (Id.) Approximately two-thirds of CTS shareholders reside outside of Indiana. (DCA App. at 59.) On March 10, 1986, DCA, then CTS' largest shareholder, commenced a tender offer for 1,000,000 additional shares of CTS stock at $43 per share (CTS App. at 1, 5), a premium of more than 20% above market price. *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 253 (7th Cir.), *appeal docketed* Nos. 86-71/86-97 (U.S. July 22, 1986). The

[9] Acquiring persons cannot compel prompt consideration of the voting rights issue by calling a special shareholders meeting under § 23-1-29-1 *et seq.* of the Business Corporation Law. First, Indiana law requires the holders of 25% of the shares to request a special shareholders meeting before it must be called by the corporation. IND. CODE § 23-1-29-2(a)(2). Many acquiring persons and most tender offerors will not have that level of share ownership. Second, Indiana law allows Indiana corporations to delay the notice of a special shareholders meeting for 60 days and forces the shareholders who called for a special meeting to then go to an Indiana court for an order compelling the corporate directors to hold a special meeting. IND. CODE § 23-1-29-3(2)(A). A mere 60 day delay subjects the "control shares" to redemption. IND. CODE § 23-1-42-10(a).

offer complied with the Williams Act and was designed to expire on April 10, 1986, 20 business days later. (DCA App. at 84.) DCA also announced a proxy campaign to elect its slate of nominees to the CTS Board of Directors at the April 24, 1986 Annual Meeting ("Annual Meeting"). (Id. at 12.)

As part of its effort to block DCA's tender offer and proxy solicitation,[10] CTS adopted the Chapter. (DCA App. at 52-57.) CTS said it would use the Chapter to remove the voting rights from the shares tendered to DCA by other shareholders. (Id. at 51; CTS App. at 34-35.) CTS also stated in filings with the District Court that it would not hold a special shareholders meeting on the voting rights issue before the Annual Meeting. (DCA App. at 50.)

Had CTS been able to enforce the Chapter, DCA could not have voted the tendered shares at the Annual Meeting. DCA therefore extended its tender offer and sought a declaratory judgment that the Chapter is unconstitutional. The District Court issued the declaratory judgment. The Seventh Circuit affirmed the District Court's decision on April 23, 1986, and DCA promptly purchased 1,000,000 of the tendered shares.

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[10] Among other things, CTS (1) invoked the Indiana Takeover Offers Act, IND. CODE § 23-2-3.1 *et seq.* (1986), by requesting a hearing before the Indiana Securities Commissioner on the adequacy of DCA's disclosures and filing an action in Indiana state court seeking to halt DCA's tender offer; (2) filed numerous counterclaims in the District Court seeking to enjoin DCA's tender offer and proxy solicitation on the grounds that, *inter alia*, DCA's disclosures were misleading and seating DCA's nominees on the CTS Board would violate Section 8 of the Clayton Act, 15 U.S.C. § 19 (1982); (3) adopted in succession three "poison pill" shareholder rights plans designed to thwart DCA's tender offer and proxy solicitation; and (4) issued false and misleading communications in connection with its adoption

SUMMARY OF ARGUMENT

This appeal arises from the actions of current management and directors (collectively "management") of appellant CTS, who, in an all-out effort to defeat a tender offer from an out-of-state bidder which complied with all federal requirements, rushed to opt into the Chapter 16 months before it became generally applicable to all Indiana corporations.At issue is whether Indiana can insulate its resident corporations from the interstate markets for corporate control, assets and securities through legislation that conflicts directly with the investor protection goals and mechanisms established by Congress in the Williams Act, 15 U.S.C. §§ 781(i), 78m(d)-(e), 78n(d)-(f) (1982 & Supp. III 1985).

The Chapter, which can be invoked by management at will, strips voting rights from the securities that put a tender offeror over certain ownership thresholds. The tender offeror can only regain these voting rights by running a statutory gauntlet of pro-management provisions.

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10 *(Continued)*

of the second poison pill. Except with respect to the second poison pill, which CTS redeemed after an unfavorable Seventh Circuit decision, *see Dynamics Corp. of America v. CTS Corp.*, 805 F.2d 705 (7th Cir. 1986), and the third poison pill, the legality of which is before the District Court, the District Court, Seventh Circuit and Indiana Securities Commissioner have rejected all of CTS' defensive measures. The following is a list of the published opinions rendered in this case by the lower courts: 805 F.2d 705 (7th Cir. 1986); 794 F.2d 250 (7th Cir. 1986), *appeal docketed* Nos. 86-71/86-97 (U.S. July 22, 1986); 1986-1 Trade Cas. (CCH) ¶ 67,134 (7th Cir. April 23, 1986); 643 F. Supp. 215 (N.D. Ill. 1986); 638 F. Supp. 802 (N.D. Ill.), *aff'd in part and vacated and remanded in part*, 805 F.2d 705 (7th Cir. 1986); 637 F. Supp. 406 (N.D.Ill. 1986); 637 F. Supp. 389 (N.D. Ill.), *aff'd* 794 F.2d 250 (1986); 635 F. Supp. 1174 (N.D. Ill.), *aff'd in part, vacated in part and remanded in part*, 805 F.2d 705 (7th Cir. 1986); [Current Binder] Fed. Sec. L. Rep. (CCH) ¶ 92, 765 (N.D. Ill. 1986).

The Chapter empowers management to delay shareholder consideration of a resolution on the voting rights issue for up to 50 days. No rational tender offeror will purchase tendered shares until the voting rights issue is resolved because of the high risk of being left without voting rights to protect its investment.

Under the Chapter's regulatory scheme, shareholders are deprived of their ability freely to tender and sell their shares to the tender offeror. In effect the Chapter subjects the individual shareholder's investment decision to the approval of three groups: management, all shareholders and all "disinterested" shareholders.

The Chapter is *per se* violative of the Commerce Clause. As admitted by Indiana and counsel for CTS, the Chapter has a protectionist purpose. The Chapter directly regulates interstate securities transactions between nonresident shareholders and tender offerors. The Chapter has substantial discriminatory effects on interstate commerce. It discriminates against nonresident tender offerors in the interstate market for corporate control, impedes the interstate flow of corporate assets, forces economic operations that might be performed more efficiently elsewhere to be performed in Indiana, and unduly shifts its burdens to unrepresented out-of-state parties.

The Chapter heavily burdens the interstate markets for corporate control, corporate assets and securities. Indiana has little to counterbalance these burdens. It has no interest in protecting out-of-state shareholders. The *post hoc* rationalizations it offers for the Chapter are flimsy at best. The extreme pro-management bias of the Chapter is inconsistent with shareholder protection and the "threats" to which the Chapter purportedly responds are illusory. Appellants draw a false analogy between tender offers and fundamental corporate changes. Indiana law already regulates the way in which the tender offeror may use its shares if it wishes to make a fundamental

change in the corporate structure.

Congress has not delegated to the states the power to interfere with interstate tender offers. To the contrary, the Chapter is preempted by the Williams Act. Congress adopted a market method of tender offer regulation that is designed to provide information to shareholders, who then are free to choose to tender and sell their shares to the tender offeror. In direct contrast, the Chapter establishes a regulatory scheme that subjects investor free choice to the "tender mercies" of management and at least two groups of shareholders.

The Chapter also conflicts with the policy of neutrality that underlies the investor protections of the Williams Act. As Congress recognized, without this policy, management will be able to subvert shareholder free choice by thwarting value-maximizing tender offers. With its pro-management weapons, the Chapter threatens the very scheme of investor protections established by Congress.

Both the District Court and the Seventh Circuit saw through appellants' characterization of the Chapter as an innocuous and isolated piece of shareholder voting legislation. They properly gauged the severe practical impact of the Chapter and concluded that it regulates tender offers in a manner that violates both the Commerce and Supremacy Clauses.

ARGUMENT

I. THE CHAPTER VIOLATES THE COMMERCE CLAUSE

The Chapter is *per se* violative of the Commerce Clause, U.S. Const. art. I, § 8, cl. 3, because (1) its acknowledged purpose is to protect Indiana companies from the interstate market for corporate control, (2) its method of achieving that purpose is the direct regulation of securities transactions between out-of-state shareholders and tender offerors, and (3) its provisions have discriminatory effects on interstate commerce. Furthermore,

the Chapter violates the Commerce Clause because its multiple burdens on interstate commerce greatly outweigh any local benefits.

Appellants' argument is driven by the assumption that if they characterize the Chapter *ipse dixit* as a harmless regulation of voting rights, it will withstand Commerce Clause scrutiny. Voting rights, however, do not exist in a vacuum. They are attached to securities that are traded in national – indeed international – markets.[11] No rational tender offeror will purchase shares without knowing whether they will include voting rights. To do so would be like buying a car before knowing whether it had an engine. Nor would any rational tender offeror buy shares lacking voting rights, leaving it unable to protect its investment. To do so would be like buying a house with no roof. By detaching the voting rights from the shares that are to be transferred in interstate tender offers, the Chapter necessarily regulates those tender offers. It chills the myriad of interstate transactions associated with each tender offer. Indeed, that is the Chapter's very purpose.

A. The Chapter Has An Unlawful Protectionist Purpose

The Commerce Clause rests on the principle that the "states are not separable economic units." *Philadelphia v. New Jersey*, 437 U.S. 617, 623 (1978), *citing Hood & Sons, Inc. v. DuMond*, 336 U.S. 525, 538 (1949). Indiana may not "place itself in a position of economic isolation." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935). As this Court has declared, "[s]hielding in-state industries from out-of-state competition is almost never a legitimate

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[11] State restrictions on international commerce are subjected to even more rigorous scrutiny. *South-Central Timber Dev., Inc. v. Wunnicke*, 467 U.S. 82, 101 (1984). The markets for corporate control, corporate assets and corporate securities are all international in scope.

local purpose. . . . " *Maine v. Taylor*, 477 U.S.___, 106 S. Ct. 2440, 2453 (1986).

Appellants concede that the Chapter is designed to shield Indiana corporations from out-of-state competitors in the interstate market for corporate control. Counsel of record for CTS stated publicly that the Chapter is intended to deter nonresidents from acquiring control of Indiana corporations:

> When asked why Indiana had decided to adopt such a virulent statute, James Strain, an Indianapolis corporate lawyer from Barnes & Thornburg says, "We don't like having all our companies taken over by East Coast firms." On further reflection, Strain says Midwestern and West Coast acquirors are no better.

3 *Corporate Control Alert* 1, 10 (March 1986) (DCA App. at 61). Indiana admits that the Chapter is a "regulation of [corporate] takeovers,"[12] (Ind. Br. at 28), which is designed to check the *"removal"* of Indiana corporations "from the State," (Ind. Br. at 90-91.) (emphasis added).[13] This Court therefore need go no further to find the Chapter *per se* unconstitutional.

B. The Chapter Directly Regulates Interstate Commerce

The Chapter is also *per se* violative of the Commerce

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[12] Indiana's statement that the Chapter is a "regulation of [corporate] takeovers" squarely contradicts its earlier assertion that the Chapter "does not govern or regulate tender offers . . . ." (Ind. Br. at 10.)

[13] The circumstances of Indiana's adoption of the Chapter further point up its protectionist purpose. The Chapter was passed after nonresidents made bids for two large Indiana corporations. 3 *Corporate Control Alert* 1, 10-11 (March 1986) (DCA App. at 61). It is part of a wave of protectionist anti-takeover legislation designed to avoid

(Footnote continued on the following page)

Clause because, like the anti-takeover act struck down in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), it directly regulates extensive interstate transactions in securities between nonresident shareholders and tender offerors. *See also Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. ___, 106 S. Ct. 2080 (1986). Direct regulation of nonresidents is inevitable because the Chapter applies even if the tender offeror, 90% of the company's shareholders, the company'smanagement and its principal place of business are located outside Indiana. Indeed, where management owns at least 10% of the corporation's stock, the Chapter applies even if *all* of the non-management shareholders and the tender offeror are from out-of-state.

By arguing that the Chapter is designed to protect

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13 *(Continued)*

this Court's decision in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982). *See generally* Block, Barton and Roth, *State Takeover Statutes: The Second Generation*, 13 Sec. Reg. L. J. 332 (1986). One of the most common forms of "second generation" anti-takeover legislation has been control share acquisition statutes similar to Indiana's in both operation and effect. Such statutes have been stricken by every court to have considered their constitutionality. *See Gelco Corp. v. Coniston Partners*, Civ. No. 3-86-847 (D. Minn. Nov. 10, 1986) (Minnesota statute); *Fleet Aerospace Corp. v. Holderman*, 637 F. Supp. 742 (S.D. Ohio), *aff'd*, 796 F.2d 135 (6th Cir.), *appeal docketed*, No. 86-344 (U.S. Sept. 2, 1986) (Ohio statute); *Terry v. Yamashita*, 643 F. Supp. 161 (D. Haw. 1986) (Hawaii statute); *APL Ltd. Partnership v. Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn.), *vacated on other grounds and appeal dismissed*, Nos. 85-5285/5286-MN (8th Cir. Nov. 26, 1985) (Minnesota statute); *Icahn v. Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985) (Missouri statute). State anti-takeover legislation often is passed in response to a bid for a state's company from an out-of-state bidder. *See, e.g., Icahn v. Blunt, supra* (bid for TWA triggered emergency passage of control share acquisition legislation).

"nondominant" shareholders from the effects of a nationwide tender offer *(see, e.g.,* CTS Br. at 34, 36), appellants have implicitly admitted that the Chapter is a direct regulation of interstate commerce. A state statute that "protects" all so-called nondominant shareholders regardless of their state of residence inevitably requires a direct and extraterritorial regulation of interstate commerce.

C. The Chapter's Effects On Interstate Commerce Are *Per Se* Unconstitutional

Appellants ignore the Chapter's devastating effects on interstate commerce. This Court has emphasized repeatedly that in Commerce Clause cases "[t]he principal focus of inquiry must be the practical operation of the statute, since the validity of state laws must be judged chiefly in terms of their probable effects." *See, e.g., Lewis v. BT Inv. Managers, Inc.*, 447 U.S. 27, 37 (1980). Even if the Chapter served legitimate, non-protectionist purposes and did so without directly burdening interstate commerce (which it does not), it would still be *per se* violative of the Commerce Clause because its provisions (1) have a substantial discriminatory effect on nonresident tender offerors in the interstate market for corporate control, thereby (2) inhibiting the interstate transfer of corporate assets (3) requiring business operations to be performed in Indiana which could more efficiently be performed elsewhere and (4) benefitting the management of Indiana corporations at the expense of unrepresented out-of-state parties.

1. The Chapter Has A Discriminatory Effect On Nonresident Tender Offerors In The Interstate Market For Corporate Control

The Chapter's burdens weigh heavily on interstate tender offers, which are a key mechanism in the operation of the interstate market for corporate control. By stripping voting rights from "control shares," the Chapter

removes all value from the tender offer transaction. Unlike other types of stock acquisitions, tender offers often are driven by the desire to purchase the element of potential corporate control that inheres in the voting rights attached to each share of common stock. Tender offerors typically pay a sizeable "control premium" to shareholders as consideration for these voting rights. *See generally* Jensen and Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON. 5 (1983). The Chapter falls more harshly upon tender offerors than upon other acquirors by stripping only the voting rights attached to the block of shares that puts a tender offeror over one of the ownership thresholds. Tender offerors purchase shares in large blocks, while other acquirors may cross a threshold through small open market or privately negotiated purchases and the like.[14]

Because it allows incumbent management to opt out of or to opt back into its provisions *after* a tender offer has been made, the Chapter imposes upon even the most intrepid tender offeror an unacceptable investment risk wholly external to the market. The opt-in/opt-out risk destroys the integrity of the securities market. Management alone has possession of material information not available to the market – whether it will in fact opt into the Chapter, opt out of the Chapter, redeem the acquiror's shares or recommend that shareholders reattach some measure of voting rights to the tendered shares. This uncertainty imposes heavy costs on the tender offeror, who must comply with the provisions of the Chapter even before they are applicable or risk finding itself in violation of state law if management opts back into the Chapter. The practi-

[14] Among all the interstate securities transactions to which the Chapter applies, tender offers are especially vulnerable to the opt-in/opt-out provision because they alone must be held open for 20 business days.

cal impact is to deter tender offers for Indiana corporations.

The Chapter's discriminatory effect on tender offers necessarily results in discrimination against nonresidents. Because the securities market is international in scope, most bidders for and shareholders of sizeable, publicly traded Indiana corporations will be nonresidents. Given the Chapter's disparate impact on out-of-state bidders and shareholders, its facial neutrality *vel non* is irrelevant. This case is no different from numerous decisions of this Court striking down facially neutral regulations which disproportionately affect out-of-state parties and impede the flow of interstate commerce. *See, e.g., Southern Pac. Co. v. Arizona*, 325 U.S. 761 (1945).

2. The Chapter Impedes The Interstate Transfer Of Corporate Assets

The Chapter also restricts the interstate transfer of corporate assets by disrupting corporate control transactions requisite to those transfers. A tender offeror who later acquires control of a corporation may shift to another state the assets of a newly acquired corporation to take advantage of a business opportunity. *See generally* Ginsburg and Robinson, *The Case Against Federal Intervention in the Market for Corporate Control*, 1986 Winter/Spring BROOKINGS REV. 9. Given its protectionist purpose, it is hardly surprising that the Chapter blocks the flow of corporate assets from Indiana to other states. The Chapter has the same impact as the statute struck down in *Hughes v. Oklahoma*, 441 U.S. 322 (1979). It restricts the out-of-state transfer of a local resource. *See also Philadelphia v. New Jersey*, 437 U.S. 617 (1978).

While the Chapter restricts the flow of corporate assets *from* Indiana to its sister states, it also inevitably curtails the flow of corporate assets *into* Indiana. After acquiring control of an Indiana corporation, some out-of-state tender offerors no doubt will transfer corporate assets into Indiana to take advantage of business oppor-

tunities or to reverse incumbent management's policy of undercapitalization. Unlike the state in *Maine v. Taylor*, 477 U.S.__, 106 S. Ct. 2440 (1986), which had compelling health and safety reasons for banning the importation of certain species of fish, Indiana has no compelling justification for restricting the importation of these corporate assets.

3. The Chapter Requires Economic Operations To Be Performed In Indiana Which Could More Efficiently Be Performed Elsewhere

The interstate market for corporate control, if unimpeded by protectionist legislation, consists of a continuing series of securities transactions which lead to transfers of control over corporate assets to parties who can make more efficient and profitable use of those assets.[15] Jensen and Ruback, *The Market for Corporate Control: The Scientific Evidence*, 11 J. FIN. ECON 5 (1983); *see also* Manne, *Mergers and the Market for Corporate Control*, 73 J. POL. ECON. 110 (1965). Where incumbent management resists such corporate control transactions, a tender offer is often the only method of maximizing shareholder wealth. *See generally* Easterbrook and Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L REV. 1161 (1981); Fischel, *Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1 (1978).[16]

[15] This market is extremely large. In 1985 there were 3,001 corporate control transactions of $500,000 or more. 3 *Corporate Control Alert* 1, 8 (April 1986) (DCA App. at 62). The total purchase price of these transactions was $179.6 billion. *Id.*

[16] The other securities transactions that may effect a change in control, such as mergers, exchange of stock and sale of the com-

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The Chapter, by its very design, allows the incumbent management of Indiana corporations to block the interstate transfer of corporate control even if the transfer would result in a more efficient use of corporate assets, increase shareholder wealth and have the support of a majority of *all* shareholders. Indiana shields its corporations from the very bidders who believe they can employ the corporate assets more profitably, thereby interrupting the natural interstate exchange of corporate control and impeding the market process toward greater performance efficiency. *See* Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 STAN. L. REV. 819, 853-854 (1981). Even if Indiana were pursuing a legitimate local interest, the Chapter's effect of forcing business operations to be performed in Indiana which could more efficiently be performed elsewhere is *per se* unconstitutional. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 145 (1970); *Toomer v. Witsell*, 334 U.S. 385, 403-406 (1948).

4. The Chapter Benefits The Management Of Indiana Corporations At The Expense Of Unrepresented Nonresident Parties

The Chapter impermissibly furthers "[e]conomic protectionism" by giving Indiana corporations "an advantage over consumers" of corporate control in other

16 *(Continued)*

pany, are largely governed by incumbent management. Only proxy challenges are initiated by shareholders and their ineffectiveness prompted the rise of tender offers. Gilson, *A Structural Approach To Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 STAN. L. REV. 819, 843 (1981). Tender offers are extended directly to the shareholders, who, protected by the Williams Act, may choose to tender their shares for sale to the tender offeror based upon their own investment criteria and without undue pressure from management or the tender offeror.

states. *Brown-Forman Distillers Corp.*, 106 S. Ct. at 2088. Indiana deputizes the management of its corporations to deprive potential nonresident acquirors of the competitive advantages they may have earned for themselves in the interstate market for corporate control through their greater efficiency, management skills and business acumen. *See Hunt v. Washington Apple Advertising Comm'n.*, 432 U.S. 333, 351 (1977). The Chapter gives to the management of Indiana corporations competitive advantages which they have failed to earn. It does so by disadvantaging nonresidents.

The Chapter's burdens fall most heavily on out-of-state parties who were not represented in the Indiana legislature. *See South-Central Timber Dev., Inc. v. Wunnicke*, 467 U.S. 82, 92 (1984); Romano, *The Political Economy of Takeover Statutes*, 41 Va. L. Rev.___(1987) (forthcoming in February, 1987). It leaves Indiana corporations free to acquire corporations in other states and to shift newly acquired corporate assets to Indiana.[17] It places no limits on the transfer out of state of Indiana corporate assets by the management of Indiana corporations, but prevents out-of-state acquirors from doing the same. Those out-of-state acquirors had no say in the Indiana legislature, even though the Chapter is a major obstacle to their obtaining control over Indiana corporations. Nor were out-of-state shareholders of Indiana corporations represented, even though the Chapter will deprive them of the premiums and the profits from efficiency gains that result from tender offers.

The primary recourse for these unrepresented parties

[17] Indeed, in 1982 CTS availed itself of the interstate market for corporate control by using a tender offer to help effect a merger between one of its subsidiaries and a Minnesota corporation. *See CTS Reports on Tender* (NEXIS, PR Newswire, Feb. 26, 1982); *CTS Corp. Acquisition* (NEXIS, PR Newswire, Jan. 11, 1982).

is to persuade their own state legislatures to pass protectionist legislation that will reverse the Chapter's effects. The Chapter thus portends a wave of retaliatory legislation. If appellants' position were law, each state would be free to "experiment," not with creative economic development programs, but with various ways to prevent nonresident tender offerors from obtaining control of resident corporations, while giving resident corporations free rein to obtain control of out-of-state corporate assets and to shift those assets to the "experimenting" state. *See Hood & Sons, Inc. v. DuMond*, 336 U.S. 525, 538-39 (1949).[18]

Appellants seek to excuse these systemic biases by claiming that potential in-state bidders for Indiana corporations "virtually" represented the interests of nonresident bidders in the Indiana legislature. (CTS Br. at 34; Ind. Br. at 85.) The number of Indiana bidders who might be burdened by the Chapter, however, is disproportionately low compared to the number of burdened out-of-state bidders. Moreover, their political influence in the Indiana legislature is weaker than that of the Indiana business interests protected by the Chapter. Indiana corporate bidders also receive a benefit from the Chapter not available to out-of-state bidders – they are shielded from bids from acquirors located in Indiana's 49 sister states. Even the resident shareholders of Indiana corporations are not likely to be as organized or as potent a force in the Indiana legislature as are the local business interests who saw the Chapter as a means of insulating Indiana corporations from the market for corporate control and keeping in Indiana corporate assets that might be utilized more efficiently elsewhere. State anti-takeover statutes are typi-

[18] CTS anticipates this argument by claiming that the state of Indiana is free to be wrong. (CTS Br. at 47.) But Indiana is not even free to be right in its experiment where, as here, it discriminates against interstate commerce.

cally the product of the local business community. *See Romano, supra.* The Chapter is no exception, 3 *Corporate Control Alert* 1, 10-11 (March, 1986).

D. The Chapter's Unnecessary Burdens On Interstate Commerce Far Outweigh Any Local Benefits

The Chapter's *per se* invalidity obviates the need for this Court to engage in any balancing of local and national interests. But even if the Chapter were not unlawful *per se*, its unnecessary burdens on interstate commerce impermissibly exceed its putative local benefits. *See Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

1. The Burdens On Interstate Commerce Are Great

Indiana has used the Chapter to "slow or freeze the flow of commerce for protectionist reasons . . . by erecting a barrier against the movement of interstate trade." *Philadelphia v. New Jersey*, 437 U.S. 617, 628 (1978); *see also Dean Milk Co. v. Madison*, 340 U.S. 349, 354 (1951). The Chapter burdens three large and vigorous interstate markets. It chills the market for corporate control by hindering the operation of a key component of that market – the tender offer mechanism. The Chapter inhibits the operation of the market for corporate assets, whose liquidity depends on transfers in corporate control. *See* Bradley, Desai and Kim, *The Rationale Behind Interfirm Tender Offers*, 11 J. Fin. Econ. 183, 183-84 (1983). The Chapter also disrupts the interstate market in securities by forcing shareholders who want to sell their shares to tender offerors to obtain the approval of at least two groups of shareholders.

This Court has recognized the harm to the national economy and shareholders nationwide when a state blocks a tender offer that complies with the Williams Act:

> Shareholders are deprived of the opportunity to sell their shares at a premium. The reallocation of economic resources to their highest valued use, a process which can improve efficiency and competition, is hindered. The incentive the tender offer mechanism provides incumbent management to perform well so that stock prices remain high is reduced.

MITE, 457 U.S. at 643.

2. The Chapter's Benefits Are Negligible

Indiana and CTS have settled on two *post hoc* rationalizations for the Chapter: (1) protection of "nondominant" shareholders, and (2) protection of local economic interests. Neither of these purported benefits would outweigh the Chapter's many burdens on interstate commerce even if they were real. But they are not.

a. The Rationale of Protecting Nondominant Shareholders Is A Pretext

This Court has already decided that a state has "no legitimate interest in protecting the nonresident shareholders." *See MITE*, 457 U.S. at 644. By claiming that its statute is designed to protect so-called nondominant shareholders *nationwide*, Indiana gives this Court little to weigh in the balance against the Chapter's burden on interstate commerce. This is particularly true because management's opt-in/opt-out exemption power is inconsistent with shareholder protection, the Chapter is not rationally related to its purported shareholder protection goal, and the Chapter is based on irrational premises.

i. Management's Exemption Power Is Inconsistent With Shareholder Protection

Like the statute in *MITE*, the Chapter allows management to invoke the Chapter to defeat a "hostile" tender

offer.[20] The Chapter will protect tendering shareholders from no one but themselves by subjecting their voluntary sale of securities to the approval of at least two shareholder groups: all shareholders and "disinterested" shareholders. Having used the Chapter to defeat a tender offer, management can exempt itself from the Chapter in order to conduct a defensive self-tender or to promote a "friendly" tender offer. In such a case, the so-called nondominant shareholders are left with what appellants would have this Court believe are the inadequate investor protections of the Williams Act. This sharp incongruity between the *post hoc* rationalization for a statute and its practical effects "tend[s] to undermine appellant's justification for the burdens the statute imposes on interstate commerce." *MITE*, 457 U.S. at 644. *See also Raymond Motor Trans., Inc. v. Rice*, 434 U.S. 429, 446-47 (1978).

ii. The Chapter Is Not Rationally Related To Its Purported Purpose

Even if the purpose of the Chapter were the protection of nondominant shareholders, the Chapter is intolerably overbroad and underinclusive. The Chapter is overbroad because it is not limited to "coercive" partial tender offers or even to all partial tender offers. It comes into play indiscriminately and applies to "any and all" tender offers, open market purchases, privately negotiated stock purchases and the full range of other share acquisitions regardless of the effect of these acquisitions on shareholders. It applies regardless of whether the share acquisition is intended to or even can lead to actual control over the operation of the corporation. Yet, it is also capriciously underinclusive because it establishes procedures by which management may exempt certain self-serving control share transactions by opting out of the Chapter.

[20] Management and shareholders have divergent interests when corporate control is at stake. *See, e.g., Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954-55 (Del. 1985) (noting the "omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders" when responding to a tender offer).

The poor fit between the Chapter and its purported purpose is even more intolerable because the Chapter is unnecessary. Other Indiana laws are tailored to prevent oppressive conduct by a large shareholder, are not triggered at the whim of management and are far less restrictive of interstate commerce. Indiana, for example, requires shareholder approval of mergers, IND. CODE § 23-1-40-3, the sale of corporate assets, IND. CODE § 23-1-41-2, and the dissolution of the corporation, IND. CODE § 23-1-45-2(b)(2). Indiana vests its shareholders with dissenter's rights. IND. CODE § 23-1-44-1 *et seq.*. Indiana allows its corporations to protect their shareholders against financially inadequate second stage transactions by adding, with shareholder approval, a fair price amendment to the corporate charter. *See Dynamics Corp. of America v. CTS Corp.*, 805 F.2d 705, ___ (7th Cir. 1986) (slip op. at 13). *See also* IND. CODE § 23-1-43-1 *et seq.* (statutory fair price amendment). "Dominant" shareholders are also restrained by the fiduciary obligations they owe to other shareholders under Indiana law.[21]

Finally, the Chapter disserves a shareholder protection purpose. It distorts shareholder choice. The Chapter gives management – which otherwise would have no direct role in the tender offer except for opining on its merits to the shareholders – the opportunity to preempt shareholder choice by wielding a formidable array of pro-management provisions against tender offers. Indeed, the Chapter permits a minority of so-called disinterested shareholders to

[21] The Williams Act as well ensures that the shareholders will know the second stage plans of the partial tender offeror by requiring the offeror to state what major changes it plans to make in the structure or operation of the corporation. 15 U.S.C. § 78m(d)(1)(C).

block a majority of shareholders from selling their shares to the tender offeror.

iii. The Chapter Is Based Upon Irrational Premises

The very notion that interstate tender offers must be heavily burdened in order to protect some shareholders against other "dominant" shareholders rests upon at least three premises so irrational that they belie the Chapter's purported purposes. The first premise is that partial tender offers are bad because they (a) sometimes result in the purchase of shares by a party who may (b) sometimes become a "dominant" shareholder and who may (c) sometimes arrange a second step transaction that may (d) sometimes yield shareholders a lower premium than they received initially. This, of course, also assumes that no statutory fair price amendment exists (as it does in Indiana, IND. CODE § 23-1-43-1 *et seq.*) or that the corporation has not adopted its own fair price amendment. Indiana's premise is not only attenuated, it is erroneous. No necessary connection exists between partial tender offers and "coercive" second-step transactions. Many partial tender offers are not followed by second-step transactions. Securities and Exchange Commission's Advisory Committee on Tender Offers, *The Economics of Partial and Two-Tier Tender Offers*, 49 FED. REG. 26755 (1984). Moreover, the empirical data show that the premiums offered shareholders in any and all tender offers exceed the sum of the premiums offered shareholders in two-step transactions by only a small margin. *Id.* at 26759.

The second erroneous premise is that stock ownership as low as 20% gives the acquiring person actual control over the corporation. Suppose, for example, four factious individuals each purchased 20% of the stock of an Indiana corporation. The Chapter would regulate each shareholder as an "acquiring person." Yet, can appellants contend with a straight face that any of these shareholders have

"control" over the corporation? And can they honestly suggest that by crossing the Chapter's 20% threshold, DCA somehow obtained "control" over CTS? The fact is that after acquiring a 27.5% ownership position in CTS through its tender offer, DCA lost its bid to seat its slate of directors on the CTS Board. By no stretch of the imagination is DCA in "control" of CTS. DCA cannot compel or block the sale or merger of CTS or force any other fundamental change in the corporation.

Finally, the Chapter irrationally assumes that "acquiring persons" pose a threat to "nondominant" shareholders. Not only is there no logical link between tender offers by an "acquiring person" and the exploitation of minority shareholders, but small shareholders typically benefit from the presence of a large shareholder. Schleifer and Vishny, *Large Shareholders and Corporate Control*, 94 J. POL. ECON. 461 (1986). Large shareholders have both the incentive to monitor aggressively management's performance and the financial resources to do so. The benefits that result from such monitoring inure to all shareholders. The presence of a large shareholder also facilitates corporate control transactions that provide shareholders with opportunities for both control premiums and increased profits from the more efficient use of corporate assets. *See generally* Holderness and Sheehan, *Raiders or Saviors? The Evidence on Six Controversial Investors*, 14 J. FIN. ECON. 555 (1985). The data show that the presence of a large shareholder typically causes an increase in the value of the company's stock. Mikkelson and Ruback, *An Empirical Analysis of the Interfirm Equity Investment Process*, 14 J. FIN. ECON. 523 (1985).

b. The Chapter Provides No Legitimate Benefit To Other Local Interests

Indiana concedes that the Chapter was motivated by its desire to protect local economic interests from the effect of interstate tender offers. (Ind. Br. at 90-91.) But, as this Court observed in *Lewis v. BT Inv. Managers, Inc.*:

> In almost any Commerce Clause case it would be possible for a State to argue that it has an interest in bolstering local ownership, or wealth, or control of business enterprise. Yet these arguments are at odds with the general principle that the Commerce Clause prohibits a State from using its regulatory power to protect its own citizens from outside competition.

447 U.S. at 43-44. If, as Indiana admits, the Chapter attempts to shield Indiana economic interests from outside competition in the market for corporate control, it is *per se* unlawful. Even if the Chapter is not *per se* unconstitutional, Indiana's interest in protecting local business does not shield the Chapter from Commerce Clause scrutiny. Indiana would have this Court weigh in its favor the economic welfare of employees, shareholders and other nonmanagement parties. The Chapter, however, does not protect these interests. It delegates to incumbent management enforcement powers and lacks regulatory standards designed to protect nonmanagement interests.[22]

3. Appellants' "Internal Corporate Affairs" Argument Is Without Merit

Appellants argue that the Chapter is an innocuous regulation of the internal affairs of Indiana corporations

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[22] The Chapter therefore is not analogous to the Maryland statute prohibiting vertically integrated petroleum producers and refiners from operating local retail outlets upheld in *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 124-25 (1978). The Maryland statute was passed not for protectionist purposes,

(Footnote continued on the following page)

that gives shareholders the right to ratify a fundamental change in the structure of the corporation by approving or disapproving a tender offer. They analogize the Chapter to provisions requiring shareholder approval of mergers and other changes in the structure of the corporation.

Appellants' analogy, however, is wrong. In rejecting this overworked analogy in *MITE*, this Court recognized that tender offers do not implicate the internal affairs of the corporation. *MITE*, 457 U.S. at 645-46.[23] Tender offers are transactions in interstate commerce between the tender offeror and shareholders through which the tender offeror assembles a block of shares. Tender offers themselves do not change the fundamental structure of the corporation. Nor do they define "relationships among or between the corporation and its current officers, directors,

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22 *(Continued)*

but in response to market data which revealed the inequitable distribution of gasoline among retailers during a period of short supply. Maryland reduced that inequity *not* by deterring all out-of-state retail competitors, but by measures precisely tailored to eliminate the inequities. The Maryland law thus permitted many interstate competitors to enter local markets.

The Chapter, in contrast, blocks all nonresident competitors in the interstate markets for corporate control and assets. Indiana admittedly protects local corporations by stopping the flow of *all* control share transactions, leaving no interstate competition. *See Lewis v. BT Inv. Managers, Inc.* 447 U.S. 27, 42 (1980). Because the Maryland statute upheld in *Exxon* left out-of-state petroleum retailers on an equal competitive footing with existing in-state retailers, that statute did not significantly affect the overall level of local competition in the industry. The Chapter, however, will depress competition between incumbent management and out-of-state acquirors for control of Indiana corporations.

[23] This Court also observed that the "internal affairs doctrine" is not a product of corporation law at all, but a "conflict of laws principle." *MITE*, 457 U.S. at 645.

and shareholders." *See MITE*, 457 U.S. at 645.

A tender offer alone does not give the tender offeror control over a corporation, but only a block of shares. Mikkelson and Ruback, *An Empirical Analysis of the Interfirm Equity Investment Process*, 14 J. FIN. ECON. 523, 550 (1985). To effect any change in the structure or control of the corporation, the offeror must exercise the voting power attached to the purchased shares. All attempts by successful tender offerors to parlay their share ownership position into control over the corporation, and especially any attempt on their part to effect a change in the corporate form, are subject to a vast range of regulations under state law. Indiana law, for example, guarantees shareholders an opportunity to elect the corporation's board of directors and to approve a merger, sale of corporate assets, dissolution of the corporation and other initiatives that directly affect the structure of the corporation.[24]

Notwithstanding appellants' dire warnings, this Court's decision affirming the Seventh Circuit would not federalize state corporate law. To the contrary, it is the Indiana legislature that has attempted to federalize its own corporate law. Even if the Chapter were construed as a regulation of the "internal affairs" of Indiana corporations, its burden on interstate commerce far outweighs the local benefits. The Chapter must fall because its method of regulating control interferes directly with the operation of the tender offer mechanism, thus discriminating against interstate commerce. The Seventh Circuit properly

[24] Shareholder approval of changes in the control over or structure of the corporation provides a critical check on the controlling party's actions in arranging transactions which implicate the corporate form. In telling contrast, Indiana law does not require shareholder approval of tender offers and other "control share" acquisitions, but leaves to management substantial discretion in applying the Chapter.

focused on the real world impact of the Chapter on interstate commerce and its decision stands for the unremarkable proposition that a state law that has a "direct, substantial and intentional" effect upon interstate commerce by interfering with the tender offer mechanism is unconstitutional. *See Dynamics*, 794 F.2d at 264.

4. Congress Has Not Delegated This Regulatory Authority To The States

Appellants' effort to derive congressional approval for the Chapter from Section 28(a) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78bb(a) (1982) must fail. That section was designed to preserve blue sky laws, which long preceded the Exchange Act and the protections of which apply only to resident investors. *See* 1 L. Loss, *Securities Regulation* 30-31 (2d. ed. 1961). As appellants well know, congressional authorization of state legislation which interferes with interstate commerce "must be unmistakably clear." *Maine v. Taylor*, 477 U.S.___, 106 S. Ct. 2440, 2448 (1986). Section 28(a), 15 U.S.C. §78bb(a), is not an "unmistakably clear" delegation to the states of the power to interfere with the interstate markets in corporate control, assets and securities.[25] Not only has Congress failed to authorize the Chapter, but it has preempted it.

II. THE CHAPTER IS PREEMPTED BY THE WILLIAMS ACT

The Chapter is preempted because it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in enacting

[25] Section 28(a) states in relevant part: "Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any state over any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations thereunder."

the Williams Act. *Hines v. Davidowitz*, 312 U.S. 52, 67-68 (1941). The Indiana legislature has established a regulatory scheme that conflicts with the execution and accomplishment of Congress' investor protection objectives.

A. The Chapter Conflicts With The Williams Act's Market Method Of Investor Protection

Even if the Chapter were designed to protect investors,[26] it conflicts with the method of investor protection selected by Congress. Congress selected a "market" method of tender offer regulation which is based upon disclosure and designed to promote investor free choice. *See generally Great W. United Corp. v. Kidwell*, 577 F.2d 1256, 1276 (5th Cir. 1978), *rev'd on venue grounds sub nom., Leroy v. Great W. United Corp.*, 443 U.S. 173 (1979). Indiana has established a paternalistic regulatory scheme that usurps investor free choice.

The Williams Act amendments to the Exchange Act were passed in 1968 to extend the federal securities laws' disclosure provisions into the largely unregulated field of tender offers.[27] In constructing legislation to accomplish its investor protection goal, Congress chose between two different methods, one based upon disclosure and the other upon externally imposed principles of "fairness" or "artificiality." *Schreiber v. Burlington N., Inc.*, 472 U.S. 1, 8 n.8 (1985). *See also Kidwell*,

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[26] As demonstrated at pages 21-25, *supra*, appellants' investor protection rationale is a pretext at best. In offering that rationale, appellants acknowledge the Chapter's repudiation of Congress' evenhanded market approach. Thus, the Chapter is defended as a means of avoiding the "unfair treatment" of shareholders. *See, e.g.*, CTS Br. at 25.

[27] Prior to the mid-1960's, corporate takeover attempts had typically involved either proxy solicitations, regulated under Section 14 of the Securities Exchange Act of 1934, 15

(Footnote continued on the following page)

supra. at 1279. Congress rejected the latter approach. *Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids: Hearings on S. 510 Before the Subcomm. on Securities of the Senate Committee on Banking and Currency*, 90th Cong., 1st Sess. 1, 198 (1967) [hereinafter Full Disclosure Hearing] (Second Statement of Manuel F. Cohen, Chairman Securities and Exchange Commission) (. . . this bill does not contemplate nor does it provide for substantive regulation of tender offers . . .)

As with its other legislation in the federal securities field, Congress concluded that the only way to protect investors without also chilling legitimate transactions (in this case, tender offers) in the underlying market was through a "calculated reliance on disclosure." *See Schreiber v. Burlington N., Inc.*, 472 U.S. 1, 8 n.8 (1985). The *MITE* plurality outlined the method of tender offer regulation adopted by Congress:

> . . . Congress intended to strike a balance between the investor, management, and the takeover bidder. The bidder was to furnish the investor and the target company with adequate information . . .

MITE, 457 U.S. at 634. The plurality also cautioned that Congress had rejected any regulatory approach that supplanted investor free choice:

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27 *(Continued)*

U.S.C. § 78n (1964), or exchange offers of securities, subject to the registration requirements of the Securities Act of 1933, 15 U.S.C. § 77e (1964). H.R. Rep. No. 1711, 90th Cong., 2d Sess., *reprinted* in 1968 U.S. CODE CONG. & ADMIN. NEWS 2811. When Congress passed the Williams Act, only Virginia had a statute regulating tender offers. Take-Over-Bid Disclosure Act, VA. CODE ANN. § 13.1-528 (1985 Replacement Volume). There is no indication that Congress was aware of the Virginia statute, which was passed only four months before the Williams Act. Nor is there any evidence in either the text of the Williams Act or its legislative history that Congress ever intended or expected states to play an active role in tender offer regulation.

> ... but there was no "inten[tion] to do ... more than give incumbent management an opportunity to express and explain its position." [citation omitted] Once that opportunity was extended, Congress anticipated that the investor, if he so chose, and the takeover bidder should be free to move forward within the time frame provided by Congress.

Id. at 634. *See also Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 58 (1975).

The Williams Act, therefore, is finely tuned to facilitate informed shareholder choice based on the investment criteria of each shareholder and the disclosures of the tender offeror and management. H.R. Rep. No. 1711, 90th Cong., 2d Sess., *reprinted in* 1968 U.S. Code Cong. & Admin. News 2811; *see also*, S. Rep. No. 550, 90th Cong., 1st Sess. (1967). The Williams Act requires both the tender offeror and management to disclose information to the shareholder erelevant to the tender offer decision. 15 U.S.C. § 78m(d). In addition, it insulates the shareholder from any external pressures affecting his or her decision whether to tender shares for sale to the tender offeror. *See* 15 U.S.C. § 78m(d)(1).[28]

The Chapter deprives individual shareholders of the free choice guaranteed to them by this federal regulatory scheme. It anoints three overlapping factions of guardians: management and at least two groups of shareholders. Each shareholder group has independent veto power over the individual shareholder's decision to sell shares to the tender offeror. The Chapter does not provide these guardians with additional tools to "protect" shareholders from the very tender offeror to whom they may have already tendered their shares. Neither the tender offeror nor incumbent management is required to make any additional disclosures that might assist shareholder guardians in making the voting rights decision. Yet, that decision will determine the tender offeror's fate.[29] If even one group of shareholder guardians rejects the tender offer, the Chapter will have undone the myriad of investment decisions of the individual shareholders.

The Chapter imposes the sort of external restrictions on shareholder free choice that were rejected by Congress. It also confounds the Williams Act's market approach to tender offer regulation by forcing shareholders to make the voting rights decision with no guarantee of adequate information. If Indiana believes that the Williams Act provides the shareholder guardians with the information necessary to make an informed decision on the voting rights issue, then the Chapter's expensive and time-consuming procedures are superfluous, albeit highly obstructive of tender offers and inconsistent with the Williams Act's approach. If Indiana believes that the voting rights decision upon which the success of every tender offer depends is an important component of the tender offer process, then the Chapter's pro-management bias and lack of disclosure requirements ill-equip it to promote informed shareholder decisionmaking and likewise conflict with Congress' market approach.

[28] Thus, tender offerors must hold open their tender offers for 20 business days, 17 C.F.R. § 240.14e-(1a) (1986), shareholders can withdraw their tendered shares during specifically established periods, 15 U.S.C. § 78n(d)(5), tender offerors must accept shares on a pro rata basis, 15 U.S.C. § 78n(d)(6), and tender offerors must pay the same consideration to all tendering shareholders. 15 U.S.C. § 78n(d)(7).

[29] Moreover, once a tender offeror has purchased shares, the other shareholder guardians have no incentive to vest the tender offeror's shares with voting rights because this would only dilute the voting power of their shares.

B. The Chapter Frustrates The Williams Act's Investor Protection Purpose By Conflicting With Its Policy Of Neutrality

The Williams Act's investor protections rest upon a careful balance struck by Congress between incumbent management and tender offerors. S. Rep. No. 550, 90th Cong., 1st Sess. 1, 3 (1967); *see also* H.R. Rep. No. 1711, 90th Cong., 2d Sess., *reprinted in* 1968 U.S. CODE CONG. & ADMIN. NEWS 2811. Congress established a policy of neutrality between management and the tender offeror as "a major aspect of the effort to protect the investor." *MITE*, 457 U.S. at 633 (plurality opinion). *See also Piper v. Chris-Craft Indus.*, 430 U.S. 1, 29-30 (1977).

Congress adopted this policy of neutrality after painstaking deliberation. Initially, the drafters of the Williams Act considered regulating tender offers by strengthening the position of both management and shareholders vis-à-vis tender offerors. Senator Williams introduced a precursor bill to the Williams Act with a message entitled "Protection Against Corporate Raiders," that decried "proud old companies [being] reduced to corporate shells after white collar pirates have seized control." S. 2731, 89th Cong., 1st Sess. 111 CONG. REC. 28257 (1965). The most potent pro-management feature of this precursor bill was a provision requiring tender offerors to disclose to management their intent to make a tender offer 20 days before commencing the offer. When coupled with a 20 business day waiting period, this provision would have given management approximately 50 days to take defensive measures against a tender offer.

But after hearing extensive testimony on the benefits of tender offers to shareholders and the success of management in defeating tender offers, *see, e.g.*, Full Disclosure Hearing, *supra*, Congress acknowledged that investors benefit from the continued operation of the tender offer mechanism. H.R. Rep. No. 1711, 90th Cong., 2d Sess., *reprinted in* 1968 U.S. CODE Cong. & ADMIN. NEWS

2811. Senator Williams disclaimed any Congressonal intent to impair the operation of the tender offer mechanism by favoring incumbent management. *See, e.g.*, 113 CONG. REC. 5854 (1967)("Every effort has been made to avoid tipping the balance of the regulatory burden in favor of management or in favor of the offeror."). Consequently, Congress removed all precommencement notification requirements from the Williams Act. Instead, Congress protected the investor "by witholding from management or the bidder any undue advantage that could frustrate the exercise of an informed choice." *MITE*, 457 U.S. at 634.[30]

The Chapter returns to management the "undue advantage" withheld by Congress. Indiana severely handicaps tender offerors by giving management its most potent defensive weapon: delay.[31] *See MITE*, 457 U.S. at 637-638. It resurrects the very 50 day window for defensive tactics that Congress expressly rejected when it deleted from the

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[30] CTS cites this very language, but then makes the inconsistent claim that the Chapter, by regulating only "post-acquisition voting rights," addresses concerns "entirely different" from ensuring that "the investor makes an 'informed choice' whether to tender his shares." (CTS Br. at 24-25.) In attempting to find some rationale for the Chapter, of course, CTS tries to convince this Court of the opposite proposition, that the Chapter has everything to do with ensuring that the investor makes an informed choice. *See, e.g.*, CTS Br. at 25, 26, 37-40.

[31] Congress recognized the harmful consequences of delay in the tender offer process when it enacted the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 1311 *et seq.* (1982) ("Hart-Scott-Rodino Act"):

> [I]t is clear that this short waiting period [the 10-day period for proration provided by § 14(d)(6) of the Securities Exchange Act, which applies only after a tender offer is commenced] was founded on congressional concern that a longer delay might

(Footnote continued on the following page)

Williams Act the 20-day precommencement notification requirement.[32] The Chapter's procedure for holding a spe-

31 *(Continued)*

unduly favor the target firm's incumbent management, and permit them to frustrate many pro-competitive cash tenders. This ten day waiting period thus underscores the basic purpose of the Williams Act–to maintain a neutral policy towards cash tender offers, by avoiding lengthy delays that might discourage their chances for success.

H.R. Rep. No. 1373, 94th Cong., 2d Sess. 12, *reprinted in* 1976 U.S. CODE CONG. & ADMIN. NEWS 2572, 2644; *see also*, 122 CONG. REC. 30877 (1976) (Statement by Representative Rodino). Incredibly, Indiana analogizes the Chapter to the Hart-Scott-Rodino Act in support of its claim that the Chapter will not interfere with tender offers. (Ind. Br. at 68-69.) Indiana ignores the fact that the Hart-Scott-Rodino Act accelerates the regulatory review process in the case of cash tender offers so that review can be completed within the 20 business day Williams Act waiting period. *See* 16 C.F.R. § 803.10(b) (1986).

32 Congress repeatedly has rejected precommencement notification provisions that would have extended tender offers beyond 20 business days. In 1965, Congress rejected a proposed 20 day prenotification requirement. *See* S. 2731, 89th Cong., 1st Sess., 111 CONG. REC. 28257, 28259 (1965). In 1967, Congress rejected a five-day prenotification requirement. S. Rep. No. 550, 90th Cong., 1st Sess. 1, 4 (1967); *Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids: Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., lst Sess. 72-75, 87-89, 98, 105, 139-40, 151, 163, 245 (1967); *Takeover Bids: Hearings on H.R. 14475 and S. 510 Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 90th Cong., 2d Sess. 1, 44-46, 50-54 (1968). In 1970, Congress rejected 30-day prenotification proposal. *See Investor Protection in Corporate Takeovers: Hearings on H.R. 4285, S. 3431 and S. 336 Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 91st Cong., 2d Sess. 1, 6-7 (1970). In 1975 Congress rejected two bills which would have required a 60-day precommencement filing. S. 2522, 94th Cong., 1st Sess., 121 CONG. REC. 32839, 32840 (1975); H.R. 10650, 94th Cong., 1st Sess., 121 CONG. REC. 35640 (1975).

cial shareholders meeting guarantees management over three additional weeks to implement a variety of defensive measures designed to thwart the tender offer. Tender offerors cannot purchase tendered shares after the expiration of the Williams Act's 20 business day waiting period. They must wait at least 50 days to buy what the shareholders tendered: an equity security with full voting rights.

The Chapter not only arms management with delay, it also:

(1) Vests management with discretion to invoke the Chapter;

(2) Increases the amount and scope of proxy materials;

(3) Subjects the shareholder's decision to sell securities to an effective veto by management and at least two groups of shareholder guardians;

(4) Permits management to redeem tendered shares pursuant to its own procedures;

(5) Raises transaction costs of making a tender offer; and

(6) Gives management complete control over the Chapter's enforcement mechanism.

Indiana argues that the Chapter is not preempted by the Williams Act because tender offerors may condition their tender offers on the eventual approval of a voting rights resolution by the shareholder guardians. (Ind. Br. at 65.) This argument ignores the fact that before the voting rights issue is resolved, management has free rein to take other defensive steps that will diminish the value of tendered shares. The same argument can be made to excuse any pro-management restriction on the tender offer process, no matter how burdensome. A tender offeror could just as easily condition its tender offer if the Chapter imposed a delay of 50 weeks rather than 50

days. But Congress did not empower the states to burden the tender offer process with delay, uncertainty and additional costs under the banner of "investor protection." Indiana's compliance manual only illustrates how tender offerors must modify substantially their tender offers from the Williams Act norm to comply with the Chapter.

CTS concedes that "Congress *itself* did not wish to 'tip the balance' " between tender offerors and management, but argues that the congressional policy of neutrality places no limits on the power of a state to impair the operation of the tender offer mechanism in order to protect the management of its corporations. (CTS Br. at 21, 22.) Appellants' Supremacy Clause argument is nothing less than the blanket assertion that Indiana has unbridled discretion to impose on the tender offer process burdens of any magnitude. Whatever role is left to the states in the field of securities regulation after over 50 years of extensive federal involvement, it certainly does not include enacting legislation which admittedly is in conflict with the Williams Act. Appellants' inverted view of federalism was repudiated by *MITE* and fails to acknowledge that Congress believed that tender offer regulation tipped in management's favor would be inconsistent with the Williams Act.

CONCLUSION

For the foregoing reasons, the decision of the Seventh Circuit Court of Appeals should be affirmed.

Dated: January 20, 1987

Respectfully submitted,

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No. 86-71

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

On Appeal From The
United States Court Of Appeals
For The Seventh Circuit

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No. 86-71

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

On Appeal From The
United States Court Of Appeals
For The Seventh Circuit

REPLY BRIEF OF APPELLANT CTS CORPORATION

Rule 28.1 Listing: The required information was provided in the jurisdictional statement of Appellant CTS Corporation at 1 n.1, and remains accurate.

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It is undisputed that the Indiana Control Share Acquisitions Chapter, in limiting the transferability of voting rights of potentially controlling corporate shares, neither (1) discriminates between interstate and intrastate commerce, nor (2) poses any threat of multiple or inconsistent burdens being placed upon commerce by the laws of different States. Appellee Dynamics Corporation of America ("DCA") therefore attacks the Chapter by firing a scattershot of Commerce Clause "theories," based on selectively quoted, out-of-context generalizations from opinions of this Court, factual assertions unsupported by any evidence, and economic and policy arguments having everything to do with legislative wisdom and nothing to do with constitutional jurisprudence.

In marked and significant contrast, the Brief for the Securities and Exchange Commission and the United States as Amici Curiae (the "U.S. Brief") takes a more balanced, reasoned approach that repudiates most of the erroneous reasoning of the Seventh Circuit, the District Court and DCA -- including any claim of Williams Act preemption. The United States nonetheless urges this Court to draw an ephemeral Commerce Clause line that would strike down the Indiana statute but leave intact a host of similar State laws that can also affect the desirability or outcome of a hostile takeover attempt. The United States' scholarly but finally unpersuasive argument demonstrates, however, that there is no constitutionally meaningful distinction between the Control Share Chapter and these other, concededly

constitutional State statutes. At bottom, the United States (no less than DCA) is inviting this Court to embark on the judicially inappropriate task of developing, under the aegis of the "dormant" Commerce Clause, a Federalized law of corporations.

I. <u>There Is No Constitutional Distinction Between the Indiana Statute and Other State Laws That Also Regulate Internal Corporate Affairs and Also Affect Hostile Takeovers.</u>

Appellant CTS Corporation ("CTS") submits as self-evident that a distinction of constitutional magnitude -- a rule that forbids discretionary choices otherwise available to the legislative branches of our State or Federal Governments -- should be capable of articulation in terms of the fundamental values of the constitutional provision invoked. The most telling feature of the DCA and U.S. Briefs is that each fails to demonstrate any

meaningful constitutional distinction, in terms of the values of the Commerce Clause, between the Indiana Control Share Chapter and a variety of other State statutes that may also adversely affect hostile takeovers but concededly raise no Commerce Clause issue. The reason for that failure is simple: No such distinction exists.

The United States disputes none of the major premises of the arguments of CTS and Indiana in support of the Chapter. It forthrightly agrees that State law is the source of whatever rights are associated with a share of corporate stock, and that the "Commerce Clause does not require a state to define in any particular way the bundle of rights that will be put into interstate commerce as corporate shares." U.S. Brief at 16 n.15. It agrees that a State's exercise of that power

> . . . does not offend the Commerce Clause, notwithstanding the obvious effects of the state's actions on the value and transferability of shares of the corporations its charters, because the chartering state is responsible for the very existence of the corporation and its shares, and it may define the latter as it wishes notwithstanding effects on their transferability.

Id. at 9-10.

The United States further recognizes that

> . . . having defined the rights of shareholders, a chartering state has an important and legitimate interest in protecting those rights with respect to all shareholders, resident and nonresident alike.

Id. at 22. Thus, unlike DCA, the United States does not tilt at the obvious fact that a State's corporation law per force "affects" -- i.e., defines, protects and regulates -- the rights of nonresident investors who purchase stock in that State's corporations, and hence per force has "extraterritorial effects" that raise no Commerce Clause concern:

> A nonresident who buys shares in an Indiana corporation accepts that state's definition of his rights and buys that state's protection.
>
> A chartering state's governance of the internal affairs of its corporations, including its definition of the rights of shareholders, obviously affects interstate commerce. Indeed, whenever the corporation then sells shares in interstate commerce, the chartering state may be said to be projecting its law beyond its borders.

Id. at 22-23 (footnotes and citations omitted).

Unlike the Seventh Circuit, the United States labors under no false belief that State laws that may make hostile takeovers less likely are for that reason constitutionally suspect. Compare U.S. Brief at 16 n.15, 23 n.24 with Seventh Circuit Opinion, CTS App. at A26 (state statute is "highly vulnerable if it impedes the important commerce in corporate control"). Hence, the United States necessarily agrees that any number of State laws

may affect the desirability or outcome of a hostile takeover attempt but raise no Commerce Clause issue whatever. See U.S. Brief at 23 n.24 (e.g., cumulative voting provisions; staggered terms for directors; restrictions on freeze-out or back-end mergers). Even DCA seems to agree that State laws of this sort are not constitutionally infirm. See DCA Brief at 23.

Finally, the United States recognizes that the voting rights of corporate shares -- the focus of the Control Share Chapter -- are also derived solely from State law. Thus, it specifically agrees that the "chartering state may define, create, and limit voting rights in ways that affect the attractiveness of shares without triggering any question under the Commerce Clause," and that "a share of stock has no inherent rights except

those that state law and the relevant corporate documents give it." U.S. Brief at 16 n.15. DCA and other amici misunderstand this point entirely, repeatedly emphasizing how "basic" and "essential" voting rights are to a share of stock. But, as the United States properly observes, the Commerce Clause imposes no constitutional "one share, one vote" rule on the States. Quaint metaphors -- a car without an engine, or a house without a roof -- cannot refute the point that a share of stock in a corporation has only those rights granted by State law.

The Indiana Chapter is, of course, just such a State law, "defin[ing] in [a] particular way the bundle of rights" reflected by a share of stock -- in a State-created corporation -- whether that share is thereafter "put into interstate commerce" or not. The

owner of that share (resident or non-resident) owns, inter alia, a proportionate share of the corporation's assets and earnings -- the first "stick" in the "bundle." Under Indiana law (and not Constitutional compulsion) the shareholder also owns, as a second "stick" in the "bundle," the right freely to transfer that "first stick" to another person. Indiana law also gives that shareholder certain voting rights in governing the corporation -- a third "stick" in the "bundle." But Indiana law further provides that the fourth "stick" in the "bundle" -- i.e., the power to transfer that voting power, whether to an in-State or out-of-State purchaser -- is not unlimited. Instead, the Control Share Chapter conditions the transferability of that "third stick" (voting power) to a potentially dominant shareholder on a

majority vote of the disinterested shareholders.

Despite its recognition of the fundamental authority of the States to create and define the voting and other rights of corporate shares, the United States nonetheless claims that the definition of voting transfer rights adopted by the Indiana statute distinguishes it from the range of other, concededly constitutional State laws. The United States reasons that the Chapter is constitutionally defective because (1) its provisions on voting rights are triggered by a purchase and sale "transaction" involving the shares; (2) although the Chapter does not discriminate between in-State and out-of-State "transactions," most (but by no means all) such transactions would take place in interstate commerce; and (3) the Chapter's "effect is

to tend to preserve whatever pattern of voting rights (and, consequently, share ownership) exists in a given corporation at a given time against transactions that would alter the pattern." See U.S. Brief at 10, 16, 19, 26, 28. The United States claims the Chapter therefore violates the Commerce Clause because, "[w]hen a share of stock defined under Indiana law to represent certain rights has lawfully entered the national marketplace in securities, Indiana may not, under the Commerce Clause, directly restrain its further transfer in the absence of a substantial state interest." Id. at 19.

Putting aside the lack of evidence on the factual links in this chain of reasoning, this formalistic focus on what triggers the Chapter ignores that "transferability" is itself one of the characteristics of a share's rights

that must be defined and regulated by State law -- as this Court has recognized in upholding a chartering State's taxation of out-of-State transfers of shares in its corporations:

> Suffice it to say that if that freedom of transfer [of Utah corporate stock] exists as respondents claim, it stems from Utah law. It finds its ultimate source in the authority which Utah has granted. It is indeed a benefit which Utah has bestowed. For it alone Utah may constitutionally ask a return.

State Tax Commission v. Aldrich, 316 U.S. 174, 180 (1942). See also Louisville & Nashville R.R. v. Kentucky, 161 U.S. 677, 702-03 (1896) (upholding State prohibition on railroad's purchase in interstate commerce of stock of competing railroad). If Indiana may tax an out-of-State transfer of the shares of its corporations, or even prohibit such transfers altogether (assuming it does not discriminate between in-State and out-of-State

transactions), then surely it may define (as it has in the Control Share Chapter) the terms under which voting rights in its domestic corporations may be transferred.

Partnership law, another area of property interests exclusively created and regulated by the States, illustrates Indiana's constitutional authority to regulate the transferability of voting rights in its domestic corporations. In the Control Share Chapter, Indiana has altered the (currently) conventional definition of corporate share rights by providing that, while the underlying interest in the corporation's assets and profits remains freely transferable, the voting right might not be transferable in a control share transaction. This differing treatment of equity interests and voting rights is no novelty -- it is

well established in the law of partnerships. While a partner may normally transfer his interest in partnership property and income, he usually may not transfer his partnership vote without the consent of other partners.[1] Such restrictions on transfer of partnership voting rights surely raise no constitutional question, whether or not the units are sold publicly and in interstate commerce. Nor can there be any meaningful constitutional distinction between partnerships and corporations. It follows that nothing in the Commerce Clause bars Indiana from restricting the transfer of voting rights in shares of corporate stock as well.

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[1]See UNIFORM PARTNERSHIP ACT § 27, 6 U.L.A. 353 (1969); REV. UNIFORM LTD. PARTNERSHIP ACT §§ 702, 704, 6 U.L.A. 259-61 (Supp. 1986).

The United States' claim that the Indiana Chapter is constitutionally impermissible because it is triggered by a "transaction" is inconsistent not only with its views on the general authority of the States over corporation law, but also with the specific example of State regulation it offers as a permissible alternative to the Chapter. The United States correctly observes that Indiana could constitutionally create corporations in which no person "may own more than 20% of the voting shares." U.S. Brief at 9. But no principled Commerce Clause distinction exists that can uphold such a law and strike down the Control Share Chapter. Under the United States' "no more than 20%" statute, the same interstate (or intrastate) "transaction" that triggers the Chapter would trigger the same loss of voting rights

whenever the share is sold to a person who already owns 20%. Moreover, the United States' "no more than 20%" statute would obviously have much the same effects in "tend[ing] to preserve whatever pattern of voting rights (and, consequently, share ownership) exists in a given corporation at a given time against transactions that would alter the pattern." Thus, the hypothetical statute the United States says is constitutional would be triggered by precisely the same "transactions" that trigger the Control Share Chapter, and would have precisely the same kind of "effects" -- the very facts that the United States says are the distinguishing features rendering the Chapter unconstitutional.

The Indiana statute is in fact far less restrictive on "transferability" in interstate (and intrastate) commerce

than the "no more than 20%" State law defended by the United States as constitutionally permissible. Rather than crudely prohibiting a transfer of voting rights that most shareholders may prefer, the Chapter allows the transfer to take place with the approval of disinterested shareholders -- the very shareholders the United States agrees "have a genuine interest in that transaction." U.S. Brief at 27. If, as the United States points out, the more restrictive statute is constitutional, then the Control Share Chapter simply must be valid as well.

The Chapter is but a nondiscriminatory exercise of Indiana's conceded power to define the property rights, including voting rights, of Indiana corporate shares. The fact that purchases and sales of shares (some or

even most of which may occur in interstate commerce) may trigger application of the Chapter is of no constitutional significance, any more than the fact that such transactions may trigger application of State laws governing mergers, share exchanges or a variety of other matters. Nothing in the Constitution requires that either an equity or voting interest in a corporation, jointly or separately, be freely transferable. In short, the Commerce Clause imposes no Platonic ideal of corporation law on the States, much less one in which all shares must have one vote and all shares and voting rights may be freely bought and sold.[2]

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[2]The United States suggests just such a Platonic ideal (and consequent Federalization) of corporation law in claiming that "a state may not confer on shareholders a right that, inherently, is not a power to govern the

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II. State Authority Over Corporation Law Is Not Limited by the Familiar Functioning of Any "National Market" for Corporate Securities.

Conceding (as they must) that the Control Share Chapter does not facially discriminate against interstate commerce or out-of-State residents, DCA and some _amici_ urging affirmance contend that the Chapter nonetheless violates the Commerce Clause because it "disrupts" or "interferes with" an inherently "national" market for

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corporation but a right to restrain interstate commerce." U.S. Brief at 12. By what standard _other_ than some idealized Federal corporation law can it be said that giving shareholders a say in the accession to power of a single dominant shareholder is not, "_inherently_," a "power to govern the corporation"? Certainly not State law standards, as the Control Share Chapter proves. _See also_ _Providence & Worcester Co. v. Baker_, 378 A.2d 121 (Del. 1977) (Delaware corporation law allows voting system in which increasing share holdings have proportionally less voting power).

corporate securities, and has a "disparate impact" on out-of-State takeover bidders. See DCA Brief at 15; Amicus Curiae Brief of the Securities Industry Association, Inc. at 3, 25. Certain strains of that theme are echoed by the United States as well. See U.S. Brief at 18, 28.

All these arguments ignore that the market for corporate securities -- however "national" its scope, and however familiar its current functioning may be -- rests entirely on property rights created and defined solely by State corporation law. In essence, DCA and supporting amici contend that, because the States have in the past generally defined share rights in ways that are now familiar, and because a familiar national market for those share rights has developed, the States are now prohibited by the "dormant"

Commerce Clause from redefining the share rights created by State laws in ways that might "disrupt" the present functioning of that market. Nothing in this Court's Commerce Clause jurisprudence supports any such contention; and this Court has rejected analytically indistinguishable claims even in the context of economic interests that, unlike the corporate share rights involved here, do not owe their very existence to the States' own laws.

Exxon Corp. v. Governor of Maryland, 437 U.S. 117 (1978), in which the Court rebuffed a Commerce Clause challenge to a Maryland law that prohibited petroleum producers and refiners from operating retail service stations, is both instructive and controlling. Although the burden of the facially nondiscriminatory Maryland law -- requiring divestment of retail stations -- fell

solely on out-of-State companies, the Court held that the statute did not violate the Commerce Clause:

> The fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce.

437 U.S. at 126. Moreover, the Exxon Court expressly rejected the "novel suggestion" that "because the economic market for petroleum products is nationwide, no State has the power to regulate the retail marketing of gas." Id. at 128. By no meaningful standard could the market for corporate securities, let alone the portion of that market involving hostile takeover bids, be said to be more "inherently national" than the market in this Nation for gasoline.

The Court rejected similar claims in Commonwealth Edison Co. v. Montana, 453 U.S. 609 (1981), which involved a

State-imposed severance tax on coal mined in the State. Some 90% of the coal was then shipped to other States, and the severance tax was passed on to out-of-State utilities and their customers. The Court rejected the claim that the tax discriminated against interstate commerce because the burden was borne primarily by nonresidents, emphasizing that "the tax burden is borne according to the amount of coal consumed and not according to any distinction between in-state and out-of-state consumers." 453 U.S. at 619.

Acceptance of DCA's "national market" and "disparate impact" theories would overturn Exxon and Commonwealth Edison, pronounce an unprecedented constitutional doctrine, and launch the courts on the mission of "Federalizing" large additional portions of the economic activity of the Nation -- not

pursuant to Congressional legislation, but rather through the "constitutionalizing," under the Commerce Clause, of the structure and operation of particular markets. Any nondiscriminatory State law would be constitutionally suspect whenever an out-of-State resident could claim that it "interfered" with the past functioning of an interstate market, or that the burden of State regulation, gauged by some nebulous standard of "fairness" that balances apples against oranges, fell "disproportionately" on nonresidents.

As CTS has pointed out, a majority of the members of this Court have repeatedly said that, absent the threat of conflicting and inconsistent burdens imposed by different State laws, the Court will not engage in obviously legislative "balancing" tasks of this sort -- such as "weighing" the "amount"

of safety accomplished by a State highway regulation against the "amount" of burden on interstate commerce. See CTS Brief at 35-37 & n.18. Nothing in those opinions or in any of this Court's Commerce Clause precedents suggests that the Federal courts may reverse that principle and engage in such legislative balancing when it is claimed that the safety benefits are enjoyed "disproportionately" by State residents, and the accompanying commerce burdens are borne "disproportionately" by out-of-State residents.[3]

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[3]This Court's Commerce Clause decisions also provide no support for DCA's related contention that the Indiana statute impermissibly "protects" incumbent management of Indiana corporations from tender offerors, most of whom (DCA asserts) will be out-of-State residents. Even if there were evidence to support the factual premises of this claim, that is not the type of protectionism between States that the Commerce Clause forbids. To

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At bottom, these "national market" and "disparate impact" claims reflect a profound misunderstanding of Exxon, Commonwealth Edison and this Court's other Commerce Clause cases. As those cases teach, the Commerce Clause is not intended to preserve the allegedly "natural" functioning of particular markets, nor to ensure that the burden of State regulation falls in equal measure on residents and nonresidents. Rather, the Commerce Clause reflects a

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whatever degree the Chapter supposedly "protects" management, it "protects" it from all hostile takeovers, not only those made by nonresidents. That is not interstate protectionism any more than was Maryland's desire in Exxon to "protect" independent service station operators from refiners. To hold otherwise would mean that whenever a State law favored one group of economic actors over another, and the less favored group contained a higher proportion of nonresidents, the State's "protection" of the favored group would violate the Commerce Clause. That has never been the law.

theory of political and economic union, under which the States are not required to further any particular economic theory, but are prohibited only from discriminating against sister States and their residents, and from burdening interstate commerce with conflicting and overlapping State regulations.[4]

Neither danger is presented by the Control Share Chapter, which is nondiscriminatory and applies only to Indiana corporations. Whatever the Chapter's "impact" on the market for Indiana

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[4]The United States rejects this view of the Commerce Clause based on Freeman v. Hewitt, 329 U.S. 249 (1949), which struck down Indiana's gross income tax as applied to out-of-State securities transactions by Indiana residents. U.S. Brief at 18 n.18. In Freeman, however, the threat of multiple State taxation of the same transactions was central to the decision, see 329 U.S. at 256-57, as the Court recognized in Armco Inc. v. Hardesty, 467 U.S. 638, 644-45 & n.8 (1984).

corporate shares, that impact threatens no Commerce Clause principle -- any more than did the impact of Maryland's regulation of petroleum products in Exxon or Montana's tax on coal in Commonwealth Edison. Moreover, the lesson of those cases is particularly compelling here, since -- unlike the claimed "inherently national" market for petroleum or coal -- the "national market for corporate control" exists at all only because the States, acting under no Commerce Clause or other constitutional compulsion, have created corporations and have thereby defined the bundle of corporate rights and interests that are available for sale in the first instance.

III. There Is Also No Constitutional Distinction Between the Control Share Chapter, Which Permits Corporations to "Opt-Out" of the Statute, and a State Law Allowing Corporations to Adopt the Same Rules in a Corporate Charter.

CTS and amici urging reversal have pointed out that the Control Share Chapter merely establishes the terms of a private contract between an Indiana corporation and its shareholders, and among the shareholders inter sese, with respect to voting rights in that corporation -- especially since IND. CODE § 23-1-42-5 allows Indiana corporations to "opt-out" of the Chapter. CTS Brief at 43 n.22; Joint Brief of the Indiana Chamber of Commerce and Indiana Legal Foundation, Inc. as Amici Curiae at 12-16. There is no substantive difference between the Chapter (which corporations may elect not to follow) and an otherwise identical statute that would authorize a corpora-

tion to adopt the Chapter's definition of voting rights as a charter provision; yet any private corporate action under the latter statute would be subject to no Commerce Clause scrutiny whatever. Despite the remarkable variety of Commerce Clause theories advanced by DCA and various amici urging affirmance, none has even attempted to respond to this point.

This Court has never held that the Commerce Clause restricts private activity, whatever the "impact" of that activity on interstate commerce. Other courts have expressly rejected the notion that action by corporate directors can violate the Commerce Clause, even though that action is authorized (as it must be) by State corporation law. Indeed, the Seventh Circuit has rejected as "frivolous" DCA's argument that Indiana law violated the Commerce

Clause by allowing CTS's board of directors to adopt a shareholder rights plan: "The commerce clause does not require states to outlaw private contracts that may impede interstate commerce." Dynamics Corp. of America v. CTS Corp., 805 F.2d 705, 718 (7th Cir. 1986). Accord, Data Probe Acquisition Corp. v. Datatab, Inc., 722 F.2d 1, 4-5 (2d Cir. 1983), cert. denied, 465 U.S. 1052 (1984); Moran v. Household Int'l, Inc., 500 A.2d 1346, 1353 (Del. 1985) (fact that directors "act pursuant to a state statute provides an insufficient nexus to the state for there to be state action which may violate the Commerce Clause").[5]

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[5]These decisions comport fully with this Court's repeated holdings that private acts authorized by State law do not constitute "State action" for Fourteenth Amendment purposes unless the statute orders the private

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In substance, the Indiana statute simply permits Indiana corporations to adopt or reject charter provisions governing the voting rights of shares. Had the Chapter been formally structured as an authorizing provision allowing its adoption by corporate election, it is plain that neither the authorization itself nor the act of corporate adoption would raise any Commerce Clause or other constitutional issue. It trivializes constitutional analysis to suggest that the result should differ simply because the Chapter, rather than requiring an affirmative "opt-in," states that its optional provisions governing voting

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acts. E.g., Flagg Bros., Inc. v. Brooks, 436 U.S. 149, 164-65 (1978); Jackson v. Metropolitan Edison Co., 419 U.S. 345, 357 (1974).

rights will apply unless an Indiana corporation "opts-out."

IV. The Indiana Statute is a Rational Exercise of State Legislative Power, Protecting the Legitimate Interests of Non-Dominant Shareholders in Indiana Corporations.

DCA and the United States also contend that the Control Share Chapter is not a "legitimate" exercise of Indiana's conceded power to govern the internal affairs of Indiana corporations. DCA's arguments on this point require no prolonged attention. In essence, what emerges from its tangle of unsupported factual assertions, economic policy arguments and out-of-context Commerce Clause cases is that DCA thoroughly disapproves of the Chapter and thinks that the Indiana legislature made a profound mistake in striking the balance among the competing interests involved. What does not emerge is any meaningful or even

coherent Commerce Clause theory under which DCA's negative views about the Chapter, which might properly be shared with the Congress or the Indiana legislature, render it invalid as a matter of constitutional law.

The United States, in this as in the other portions of its argument, takes a more reasoned approach that candidly acknowledges State power in this area. It agrees that Indiana has

> . . . a legitimate and substantial interest in governing the "internal affairs" of its corporations, including the rights of shareholders vis-à-vis the corporation itself, its directors and officers, and fellow shareholders.

U.S. Brief at 22. It further agrees that the State may (indeed, must) project these aspects of its corporation laws to nonresident shareholders and others who choose to deal with the corporation, id. at 22-24, and that the State may regulate internal corporate

affairs in ways that may promote or restrict hostile takeovers, id. at 24-25. Finally, the United States observes that "Indiana is quite correct that other shareholders may have a genuine interest in [a] transaction" that creates or transfers a substantial block of control shares. Id. at 27.

The United States then advances, however, an arbitrary limit to this conceded State authority, and argues that the Control Share Chapter falls outside it. The proposed boundary is that mergers, acquisitions, and "other 'fundamental changes' that generally require shareholder approval are changes in the very structure of the corporation," id. at 25 & n.28, whereas tender offers involve only shareholders and third parties, id. at 25-26.

This distinction -- also advanced in DCA's Brief at 27-28 -- ignores the practical consequences of a control share transaction. Furthermore, the distinction has no basis in any source of Federal law, let alone the Commerce Clause. As a practical matter, a control share transaction obviously affects "the rights of shareholders vis-à-vis . . . fellow shareholders," thereby squarely fitting the United States' own definition of "internal affairs." U.S. Brief at 22. Far more important, however, is that State corporation law -- and only State corporation law -- determines which corporate transactions or events are sufficiently "fundamental" that shareholder approval should be required.

Short of a decision by Congress to "Federalize" corporation law -- a step it has consistently refused to take --

the States are the only arbiters in our Federal system of the rules of corporate governance, including the rules governing share voting rights and which matters are sufficiently "fundamental" to require a shareholder vote. Whatever academic views the United States, DCA, CTS or even this Court may have on whether a given corporate transaction "should" be submitted to shareholders in a "model" corporation statute, the Commerce Clause does not impose any ideal form of corporation law upon Indiana and its sister States. The United States and DCA offer no explanation whatever of how their view of what constitutes a "fundamental" corporate event can be derived from the Commerce Clause.

Protecting small shareholders from coercive takeover tactics and potential abuses by dominant shareholders estab-

lishes a rational basis for the Indiana legislature's judgment in enacting the Control Share Chapter -- namely, that the practical consequences of control share transactions for other shareholders are so important and "fundamental" that they should be allowed to vote on a proposed change in voting control. See CTS Brief at 25-26, 37-39; Indiana Brief at 88-89. CTS does not claim that Indiana's views on these issues reflect the only possible or reasonable conclusion; but CTS, unlike DCA and the United States, is not contending (and need not persuade this Court) that Indiana's is the only conclusion permitted by the United States Constitution. CTS's contentions are far more modest, but no less dispositive: The Indiana legislature's judgment is rationally supportable; and whoever may have the better of the

economic and other policy debates about the wisdom of that judgment, our constitutional system of Federalism establishes that the judgment was Indiana's to make.

V. The United States and the SEC Have Shown That the Indiana Statute Is Not Preempted by the Williams Act.

The United States and the Securities and Exchange Commission (the "SEC") give short shrift to DCA's claims that the Control Share Chapter is preempted by the Williams Act, effectively undermining any plausible basis for maintaining that contention. The SEC, the Federal agency responsible for administering and enforcing the supposedly conflicting Federal statute, agrees that there is no conflict between the provisions of the State and Federal laws, and that the Indiana Chapter violates no preemptive Federal statutory policy. Neither DCA nor other

amici urging affirmance have pointed to any conflict in the statutory provisions, and their asserted conflict with Federal "policy" is disavowed by the Federal Government itself.[6]

The SEC may claim that it has the authority, under the Williams Act, to promulgate regulations that would preempt the Control Share Chapter. Regardless whether such a claim would be correct, it conclusively demonstrates that the Chapter is not now preempted. If the Williams Act does not give the SEC authority to promul-

[6]The futility of DCA's preemption claim is underscored by the fact that the source of the Federal 20 business day minimum waiting period for tender offers -- the centerpiece of DCA's efforts to posit a "conflict" with the Control Share Chapter -- is not the Williams Act itself but a regulation promulgated by the SEC. 17 C.F.R. § 240.14e-1(a) (1986). The SEC, however, has advised the Court that there is no conflict between its regulation and the Indiana statute.

gate regulations that would override the substantive provisions of the Indiana statute -- an issue that this Court need not decide -- then the Chapter cannot be preempted by the Williams Act. If, on the other hand, the SEC does have has such authority but has declined to exercise it, then the Chapter has not been preempted. In either event it is plain, as the United States and the SEC agree, that DCA's preemption claim in this case is meritless.

VI. Conclusion.

Though DCA and the United States both contend that the Control Share Chapter is somehow outside the constitutional pale, neither can articulate any meaningful constitutional theory as to why this should be so.

Plainly, Indiana has, in enacting the Chapter, exercised its power to define and regulate corporate voting rights in a way that differs from the pattern followed by most States, at least in recent decades. Plainly too, DCA is outraged and the United States is somewhat troubled by this departure from what each apparently considers the "norm" of "modern" corporation law. But "modern" corporation law, including such features as "one share, one vote" and freely transferable equity and voting interests, is itself a fairly recent phenomenon in our Nation's history. What is far more important, in terms of the issue presented to this Court, is that the Commerce Clause does not engraft these or any other features of State corporation law into the Federal Constitution -- regardless how "natural" such features may now seem to

DCA or anyone else; regardless whether a familiar "national market" may have developed in corporate shares as previously defined by Indiana or its sister States; and regardless whether the legislative judgment embodied in Indiana's departure from those previous definitions reflects a "wise" or even a "good" resolution of any underlying economic and other policy debates.

The Commerce Clause simply does not establish any substantive norms of corporation law that limit the States in enacting nondiscriminatory laws like the Control Share Chapter. In holding the Chapter invalid, the Seventh Circuit read its own economic and corporate governance theories into the "dormant" Commerce Clause -- just as it read into the Williams Act its own views of proper "neutrality" in take-over contests. The United States

properly disclaims the lower court's preemption reasoning, and offers a less sweeping set of corporate governance ideals to which it claims the States must constitutionally adhere. In substance and effect, however, the United States is asking this Court to do, albeit on a more limited scale, precisely what the Seventh Circuit did -- Federalize State corporation law.

The judgment below should be reversed.

Respectfully submitted,

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JOINT BRIEF OF THE INDIANA CHAMBER OF COMMERCE AND INDIANA LEGAL FOUNDATION, INC. AS *AMICI CURIAE* IN SUPPORT OF APPELLANTS CTS CORPORATION AND THE STATE OF INDIANA

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DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

JOINT BRIEF OF THE INDIANA CHAMBER OF COMMERCE AND INDIANA LEGAL FOUNDATION, INC. AS *AMICI CURIAE* IN SUPPORT OF APPELLANTS CTS CORPORATION AND THE STATE OF INDIANA

The Indiana Chamber of Commerce and Indiana Legal Foundation, Inc. respectfully submit this joint brief as *amici curiae* in support of Appellants CTS Corporation and the State of Indiana, with the consent of the parties, to urge the Court to reverse that part of a decision by the United States Court of Appeals for the Seventh Circuit which held that portions of the Indiana Business Corporation Law were unconstitutional under the Supremacy Clause and the Commerce Clause.

STATEMENT OF INTEREST

The Indiana Chamber of Commerce ("Indiana Chamber") is the largest association of businesses in Indiana, having more than 4,500 business firms as members. A very large percentage of these members are firms organized and doing business as corporations under the laws of Indiana. Some are corporations publicly traded on securities exchanges, others are not traded on exchanges but have enough shareholders to be subject to the statutory provisions at issue in this case, and still others are closely-held corporations. Indiana Legal Foundation, Inc. ("Foundation") is a private, not-for-profit corporation that represents a group of business and industrial concerns from across the State of Indiana in litigation involving broad and significant legal questions.

The Indiana Chamber and the Foundation are concerned about this case because they believe the State of Indiana should have a general corporation statute that has as one of its primary goals the fair treatment of corporate shareholders *as a whole* and that allows members of corporate management to pursue the type of business strategy that they, as the *elected* representatives of the shareholders, deem to be in the best overall and long-range interests of the corporation and its shareholders. One of the State's tools for effecting these goals, the Control Share Acquisitions Chapter, Ind. Code Ann. § 23-1-42-1, *et seq.* ("Control Share Chapter"), was effectively declared

unconstitutional on its face by the United States Court of Appeals for the Seventh Circuit. The entire Indiana Business Corporation Law ("IBCL"), of which the Control Share Chapter is but one small part, was prepared in 1985 by the Indiana General Corporation Law Study Commission, and the Indiana Chamber assisted the Commission in the process of developing ideas for and drafting the IBCL in part because the Indiana Chamber's members favored the type of fair and reasonable provisions that are set forth in the Control Share Chapter. Neither the Indiana Chamber nor the Foundation support any unfair treatment of tender offers. In fact, the Indiana Chamber has members who would not want to be precluded from making tender offers for Indiana corporations.

SUMMARY OF ARGUMENT

The Control Share Chapter does not regulate the purchase and sale of shares in tender offers, which is the subject of the Williams Act. The Control Share Chapter establishes, in effect, a permissive corporate charter provision which governs the voting rights of shares under certain change of control circumstances. The validity of shareholder rights charter provisions is invariably determined on the basis of state law. Attempts by Congress to adopt legislation regulating shareholder rights charter amendments have thus far failed.

As the Control Share Chapter is the functional equivalent of a shareholder rights charter amendment, and as shareholder rights amendments are immune from constitutional attack, the Seventh Circuit's holding has created the anomaly that Indiana is forbidden to automatically include the Control Share Chapter in charters of its domestic corporations (subject to a corporation's right to opt out of the Control Share Chapter), but is free to invite its domestic corporations to adopt the identical provisions *with impunity* on their own. Not only is this result illogical, but it conflicts with the traditional

right of a state to govern the relationships among its corporations and their officers, directors and shareholders. The line should be drawn on preemption by the Williams Act between statutes that regulate the purchase and sale of shares in tender offers and those that do not.

In applying the benefit/burden test of *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), under the Commerce Clause, the Seventh Circuit adopted its own economic theory to demonstrate conclusively that any putative benefits to legally cognizable Indiana constituencies would be insignificant. The *amici*, on the other hand, believe that there are real and substantial benefits from the Control Share Chapter for Indiana corporations and their shareholders, officers and directors. This disagreement illustrates the dispute among those who have given serious thought to the issues in the tender offer debate. The *amici* believe that in the absence of any evidence of the Control Share Chapter's effect on Indiana constituencies and in the absence of federal legislation, the Court should defer to the policy decision of the State of Indiana, in accordance with the presumption of the constitutionality of state statutes in areas traditionally regulated by the states.

Finally, the *amici* believe that a close examination of the operation of the Control Share Chapter leads to the conclusion that it will not in any way preclude tender offers for Indiana corporations. Several strategies for conducting a tender offer, consistent with the Control Share Chapter, are evident.

ARGUMENT

The overarching issues before the Court in this case are (a) whether federal law so dominates the tender offer arena that any state action having some effect on tender offers violates the Supremacy Clause of the United States Constitution, even if it is an action traditionally within the exclusive province of the states, and (b) whether the appellate court's benefit/burden analysis under the

Commerce Clause of the United States Constitution, which amounts to a judicially enunciated national policy opposing state statutes that affect tender offers, will be approved. The Control Share Chapter has been labeled by the Seventh Circuit as an anti-takeover statute and a "lethal dose" for takeovers of Indiana corporations by hostile tender offers. Appendix to Jurisdictional Statement of Appellant CTS Corporation ("CTS App.") at A23. Unquestionably, the Control Share Chapter *affects* tender offers under certain circumstances. After all, it may be inferred from the language of the Control Share Chapter and of other shareholder protection provisions of the IBCL that the Control Share Chapter was adopted to correct perceived abuses. However, the Control Share Chapter does not *regulate* tender offers, and the real and substantial benefits the Control Share Chapter provides to Indiana shareholders outweigh any incidental effects it may have on tender offers for the shares of Indiana corporations.

The Indiana Chamber and the Foundation will not repeat in this brief the analyses of CTS Corporation and the State of Indiana demonstrating that the Control Share Chapter does not violate either the Supremacy Clause or the Commerce Clause. The Indiana Chamber and the Foundation will focus instead on three points they believe to be particularly significant in evaluating those analyses. They believe, first, that the Control Share Chapter is in the nature of a shareholder rights charter provision operative only *after* a control share acquisition and, therefore, cannot be preempted by the Williams Act. Secondly, they believe that the Control Share Chapter provides substantial benefits and that, in the absence of federal legislation, the presumption of the constitutionality of state statutes in traditionally state-regulated areas should govern rather than the unsubstantiated economic theory of the Seventh Circuit. And, finally, the Indiana Chamber and the Foundation are convinced that a careful analysis of the Control Share Chapter reveals that its presumed role in

deterring tender offers is materially overstated. This brief is intended to underline, from a public policy perspective, the conclusions that CTS Corporation and the State of Indiana reach following more traditional Supremacy Clause and Commerce Clause analyses.

I. The Control Share Chapter is in the Nature of a Shareholder Rights Charter Provision and is not Preempted by the Williams Act.

As the operation and effect of the Control Share Chapter are essentially the same as many types of shareholder rights charter provisions and the Control Share Chapter is not concerned with the activities regulated by the Williams Act, it is both illogical and improper to conclude that the Williams Act preempts the Control Share Chapter.

A. The Control Share Chapter does not Regulate the Purchase and Sale of Shares and, Therefore, is not Preempted by the Williams Act.

The Control Share Chapter does not in any way regulate the buying and selling of shares in a tender offer or otherwise. The Control Share Chapter in effect does nothing more than establish a permissive corporate charter provision which governs the voting rights of shares under certain change of control circumstances. Shares of any public Indiana corporation subject to the IBCL are subject to the provisions of the Control Share Chapter, unless the corporation opts out,[1] as part of the share contract. The Control Share Chapter thus defines certain of the rights of shares, and it is the bundle of share rights, the share contract, which is bought and sold in the market.

[1] The effective date of the IBCL is August 1, 1987. However, before its effective date a corporation may, under Ind. Code Ann. § 23-1-17-3(b), elect to have most of its provisions, including the Control Share Chapter, apply to it. At any time, a corporation may elect under Ind. Code Ann. § 23-1-42-5 not to be governed by the Control Share Chapter.

Generally, the Williams Act regulates the purchase and sale of corporate shares by means of tender offers, not, as the Seventh Circuit stated, the "interstate traffic in corporate control." CTS App. at A24; *see Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 22-24 (1977) (summarizing the Williams Act); *Edgar v. MITE Corp.*, 457 U.S. 624, 632 (1982) (also briefly summarizing the Williams Act). For example, where a battle for corporate control has nothing to do with the buying and selling of shares in a tender offer, such as in a proxy contest or an open-market stock accumulation,[2] the Williams Act is wholly inapplicable.

The Control Share Chapter differs fundamentally from other state statutes which are sometimes denominated "control share acquisition" statutes. The Control Share Chapter affects how control shares are treated *after their purchase* in relation to other shares of the corporation, rather than regulating in any way the purchase or sale of shares in the first instance. This sets the Control Share Chapter apart from the Williams Act and is the heart of the distinction between the area covered by federal tender offer regulation and traditional state corporate law. The governance of tender offers and the governance of internal corporate matters have never been held to intersect. *See Edgar v. MITE Corp.*, 457 U.S. 624, 645-646 (1982) (the "internal affairs doctrine" was of no avail to supporters of an Illinois takeover statute because the statute regulated the buying and selling of shares, not the relationships among or between the corporation and its officers,

[2] For a discussion of a successful application of this emerging takeover technique, *see* Hertzberg & Rundle, *Campeau's Victory in Battle for Allied Signals Big Changes in Takeover Tactics*, Wall St. J., Nov. 4, 1986, at 2, col. 3.

directors and shareholders).[3] The Control Share Chapter is the functional equivalent of a shareholder rights charter provision governing voting rights, and the adoption of any such provision is an internal corporate matter.

B. Shareholder Rights Charter Provisions are Regulated Solely by State Law.

The remarkable increase in tender offers in recent years has led to the development of a wide variety of provisions in corporate charters and by-laws adopted for the purpose of making corporations less attractive takeover candidates and to ensure fair treatment of non-tendering shareholders in the event of a takeover. Winter, Stumpf & Hawkins, *Shark Repellents and Golden Parachutes: A Handbook for the Practitioner*, at 3-5; Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 Harv. L. Rev. 1693, 1744 (1985). Provisions in use today range from staggered terms for members of the board of directors to provisions for the issuance of bargain-price securities to shareholders in the event of a control share acquisition, which are sometimes referred to as "poison pills."[4] *See, generally*, Securities Exchange Act Release No. 15230 (October 13, 1978), [1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,748; Wander & LeCoque, *Boardroom Jitters: Corporate Control Transactions and Today's Business Judgment Rule*, 42 Bus. Lawyer 29 (November 1986); Winter, Stumpf & Hawkins, *Shark Repellents*.

[3] All of the post-*MITE* cases in which takeover statutes have been struck down under the Supremacy Clause have involved statutes that restricted in some way the purchase of shares. None considered the issue of voting rights apart from stock ownership. *Icahn v. Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985); *APL Limited Partnership v. Van Dusen, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985); *Fleet Aerospace Corp. v. Holderman*, 796 F.2d 135 (6th Cir. 1986).

[4] For consistency, such provisions, whether amendments to or original provisions in corporate charters, articles of incorporation or by-laws, will hereinafter be referred to as "shareholder rights provisions."

The courts have analyzed the legality of these provisions on two levels: First, whether the adoption of the amendment by the board and/or the shareholders was authorized by a state enabling statute (which is typically the state's general corporation statute), or was without statutory authorization and, therefore, illegal or *ultra vires*. Second, whether the board violated its fiduciary duty to the shareholders by adopting an amendment unfair to the shareholders and tending to entrench the incumbent management, or acted in good faith in the best interests of the corporation and its shareholders.

In *Moran v. Household International, Inc.*, Del, 500 A.2d 1346 (1985), the Delaware Supreme Court upheld the adoption of a complicated "poison pill" charter amendment pursuant to which Household's shareholders would receive the right to buy preferred shares in Household or common shares in the corporation surviving a hostile merger with Household at a discounted price in the event of the acquisition or the threatened acquisition of control shares of Household. After concluding that the board had authority to adopt the amendment under the Delaware General Corporation Law and that the provisions giving that authority were not preempted by the Williams Act and did not violate the Commerce Clause, the court held that the board adopted the plan "in the good faith belief that it was necessary to protect Household from coercive acquisition techniques," and not for the purpose of entrenching itself. *Id.* at 1357. Therefore, the board's adoption of the shareholder rights plan did not violate its fiduciary duty to the shareholders.

In *Minstar Acquiring Corp. v. AMF Inc.*, 621 F. Supp. 1252 (S.D.N.Y. 1985), the target corporation's board adopted a number of shareholder rights provisions, including a "poison pill." The court (applying New Jersey law) found that the "poison pill" amounted to a major change in the structure of the corporation's capitalization and in shareholder voting rights and, consequently, could

only be approved with a shareholder vote. *Id.* at 1259. The board's adoption of the "poison pill" without the shareholders' approval was an *ultra vires* act. *Id.* The court also held that the non-transferability of the rights package issued to shareholders after the tender offer trigger was an unreasonable restraint on alienation of property and, therefore, illegal under New Jersey law. *Id.* at 1258.

Although shareholder rights provisions often have the effect of deterring tender offers, their validity is invariably determined on the basis of state law. For reasons which will be discussed *infra*, statutory provisions enabling the adoption of shareholder rights amendments have not been successfully challenged under the Supremacy Clause. Congress has so far been unwilling to enter into the regulation of shareholder rights provisions. For example, recent efforts to nullify the business judgment rule — which promotes adoption of defensive measures by creating the presumption that board actions have been taken in the best interests of the corporation and its shareholders — by federal legislation have failed. *See* ABA Securities Regulation Committee, *Annual Review of Federal Securities Regulation*, 40 Bus. Lawyer 997, 1017 (1985) (discussing H.R. 5695, 98th Cong., 2d Sess. (1984)). Corporate boards today may adopt shareholder rights amendments unrestricted by federal law and, by virtue of the business judgment rule, with a limited amount of protection in most states against being second-guessed by the courts as to their motives.

C. The Control Share Chapter is Equivalent to a Moderate Shareholder Rights Charter Provision.

The Control Share Chapter shares characteristics with various types of shareholder rights provisions. For example, a Delaware corporation's charter contained a control shares voting provision very similar in effect to the Control Share Chapter in *Providence & Worcester Co. v. Baker*, Del., 378 A.2d 121 (1977). The Delaware Supreme

Court upheld the charter provisions as consistent with the state's general corporation statute.[5] The voting plan in *Providence & Worcester* provided that each common share up to 50 for each shareholder had one vote, and each common share in excess of 50 for each shareholder had one-twentieth of a vote. In addition, no shareholder could vote more than 25% of the total number of voting shares except by proxy. As with the Control Share Chapter, shares had different voting rights depending on which shareholder held them. Plans similar to the charter provisions in *Providence & Worcester* were upheld under Iowa law in *Kersten v. Pioneer Hi-Bred International, Inc.*, 626 F.Supp. 647 (N.D. Iowa 1985), and found to be *ultra vires* under New Jersey law in *Asarco Inc. v. Court*, 611 F. Supp. 468 (D. N.J. 1985). In each case, the plan's validity was determined pursuant to state law, not the Williams Act.

The shareholder rights plan at issue in *Moran v. Household International, Inc.*, Del., 500 A.2d 1346 (1985), provided, among other things, for the issuance of one "right" per common share to pre-acquisition shareholders in the event any single entity or group acquired 20% or more of Household's shares. A "right" was exercisable to purchase a fractional share of preferred stock, or, in the event of a subsequent merger, a "right" could be exercised to purchase $200 of the common stock of the survivor for $100. The plan did not prohibit or restrict in any way the purchase of shares by a tender offeror. Both the Control Share Chapter and the shareholder rights plan in *Moran* concern the treatment of shares *after their purchase* in relation to other shares of the corporation. Unlike the shareholder rights plan, however, the Control Share Chapter permits the post-acquisition dilution of voting rights to be reversed by a simple majority of the shareholders.

[5] The lawsuit did not arise in connection with a tender offer. The only issue was whether the charter provisions were authorized by the state statute.

In cases such as these, courts struggle to find the proper balance between the right of shareholders to have unobstructed access to tender offerors and the legitimate concern that not all tender offers are in the best interests of the shareholders as a whole. Indiana endured the same struggle in crafting the Control Share Chapter and resolved it by giving the shareholders the right to determine whether control of the corporation will change.

D. Eliminating the Control Share Chapter While Permitting Similar Provisions as Charter Amendments is Illogical and not Required by the Williams Act.

Although the Control Share Chapter and several types of shareholder rights provisions may operate very similarly and produce similar results, the Control Share Chapter is an explicit provision of a state statute, and charter amendments are adopted by boards of directors (sometimes with and sometimes without shareholder approval). The court in *Moran v. Household International, Inc.*, Del., 500 A.2d. 1346, 1353 (1985), rejected the argument that the provisions of the Delaware General Corporation Law authorizing the shareholder rights plan at issue were preempted by the Williams Act. The court held that the action of a board of directors in adopting a shareholder rights amendment is a private action. *Id.* The fact that the adoption took place pursuant to a state statute did not provide a sufficient "nexus" to the state to constitute state action in conflict with the Williams Act. *Id.; see also Data Probe Acquisition Corp. v. Datatab, Inc.*, 722 F.2d 1, 5 (2d Cir. 1983), *cert. den.*, 465 U.S. 1052 (1984); *Schreiber v. Burlington Northern, Inc.*, 472 U.S. ____, 86 L.Ed.2d 1, 9 (1985) (provisions of the Williams Act not "an invitation to the courts to oversee the substantive fairness of tender offers. . ."). The consequence of these holdings is simply to

immunize shareholder rights provisions from constitutional attack.[6]

Combining the *Moran* decision with the Seventh Circuit's decision in this case creates the anomaly that a shareholder rights provision, no matter how much it operates to discourage or even eliminate the possibility of tender offers, will be judged solely on state law grounds, while the same provision, if effectively included in the corporation's charter by statute, will be judged by its compliance with the Williams Act. Indiana could spell out the terms of the Control Share Chapter in the State's general corporation statute as a charter amendment that boards of directors of Indiana corporations would be *authorized* to adopt, and provide that its adoption would not constitute a breach of the board's fiduciary duty to the shareholders, and the provision would be immune from Supremacy Clause challenge.[7] In that case, the only

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[6] The *Moran* court did not decide the question of whether the Williams Act would have preempted the shareholder rights plan at issue if there had been state action connected with its adoption.

[7] It is well established that a state has the right to determine the fiduciary duties of corporate directors, and, consequently, to eliminate them in connection with certain actions. *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 479 (1977) (fiduciary standards with respect to corporate transactions vary from state to state and applying a "federal fiduciary principle" would overlap and possibly interfere with state corporate law); *Cort v. Ash*, 422 U.S. 66, 84 (1975) (state fiduciary standards put shareholders on notice of which duties directors of their corporations have and which duties they do not have).

It is probably inaccurate to speak of the duties of corporate directors as "fiduciary duties," as if directors were subject to the same duty of care as trustees. Kaplan, *Fiduciary Responsibility in the Management of the Corporation*, 31 Bus. Lawyer 883, 886-888 (1976). In fact, the duty of care and the duty of loyalty owed by directors to shareholders are simply two of many duties of corporate directors set forth at common law, in state statutes and even in some federal statutes. State general corporation statutes vary considerably in the

(Footnote continued)

difference from the Control Share Chapter would be that the board would have the choice to opt in to the provision rather than the choice to opt out. The shareholders would have the same level of protection under either scenario, because the State, the directors, and the shareholders themselves would all be deciding what is in the best interests of the shareholders as a whole.

(Footnote continued)

myriad of duties required of directors and in the standards to which directors are held in performing those duties. It is not unprecedented for a state to relieve directors from liability for actions "traditionally" (*i.e.*, at common law or under a prior general corporation statute) the responsibility of the board of directors. *See, e.g.*, McKinney's N.Y. Bus. Corp. Law § 620(f) (charter provision placing certain board duties in the hands of the shareholders, subject to the consent of all of the shareholders, relieves directors of liability for negligence in the performance of such duties).

The IBCL, a comprehensive corporate statute of which the Control Share Chapter is but one of many integral parts, contains numerous other provisions changing directors' duties and liabilities from those under prior law. For example, the statute provides that directors will not be liable for any action or failure to take action unless the director has breached or failed to perform certain enumerated duties and such breach or failure to perform constitutes *willful misconduct or recklessness* (Ind. Code Ann. § 23-1-35-1(a) and (e)); that directors may, in considering the best interests of a corporation, consider the effects of an action on shareholders, *employees, suppliers and customers of the corporation, and communities in which offices or other facilities are located* (Ind. Code Ann. § 23-1-35-1(d)); that a corporation has much broader powers to indemnify an individual and advance expenses if that individual is made party to a proceeding because the individual is or was a director (Ind. Code Ann. §§ 23-1-37-1 through 15); and that the directors are empowered to establish a corporate committee to determine whether it is in the best interests of the corporation that a proceeding be continued in which the rights of the corporation are asserted derivatively (Ind. Code Ann. §§ 23-1-32-1 through 5). Delaware has also recently modified its general corporation statute to allow shareholders to include in the corporate charter a provision limiting directors' monetary liability for certain types of breaches of fiduciary duty. Del. Gen. Corp. Law § 102(b)(7).

It is difficult to believe that the intent of the Williams Act was to give constitutional significance to the trivial distinction between the way Indiana actually chose to exercise its prerogatives and the way it could have exercised them. The fact that the adoption of the Control Share Chapter is consistent with a state's traditional right to govern the relationships among its corporations and their officers, directors and shareholders makes the anomaly even harder to accept. *See Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 478-479 (1977) ("Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden"); *Cort v. Ash*, 422 U.S. 66, 83-85 (1975) ("Corporations are creatures of state law, and investors commit their funds to corporate directors on the understanding that, except where federal law expressly requires certain responsibilities of directors with respect to stockholders, state law will govern the internal affairs of the corporation").

By no means do the *amici* favor all shareholder rights provisions. They do favor the type of provisions contained in the Control Share Chapter, because they are tempered and fair. The question the *amici* pose is whether the Williams Act was ever intended to grow to so dominate the tender offer arena that the traditional right of states to enact such provisions concerning the internal affairs of their domestic corporations would be in peril.

There is no evidence that the Williams Act was intended to prevent a state from effectively inserting into the charters of its corporations a shareholder rights provision that it could just as easily have permitted corporate directors to adopt on their own *with impunity*. The State's action is consistent with the traditional right of states to govern the internal affairs of their domestic corporations and is not inconsistent with the Williams Act's regulation of

buying shares in a tender offer. A line has to be drawn somewhere on the preemptive power of the Williams Act. The Indiana Chamber and the Foundation believe that to be logical and consistent with over 160 years of jurisprudence, from *Trustees of Dartmouth College v. Woodward*, 17 U.S. (4 Wheat.) 518 (1819), to the present, the line should be drawn between statutes that regulate the purchase and sale of shares in tender offers and those that do not. Such a rule would be consistent with the text of the Williams Act, its legislative history and its interpretation by this Court. At the same time, it would not imperil the traditional role of the states in governing the internal affairs of their domestic corporations. Under such a rule, there would be no constitutional conflict between the Williams Act and the Control Share Chapter.

II. The Control Share Chapter Produces Significant Benefits, and any Burdens it Imposes on Interstate Commerce are Negligible.

The heart of the Seventh Circuit's holding that the Control Share Chapter is unenforceable by reason of the Commerce Clause is that the Control Share Chapter impairs the interstate market for corporate control. In its most telling statement, the Seventh Circuit said:

> "Even if a corporation's tangible assets are immovable, the efficiency with which they are employed and the proportions in which the earnings they generate are divided between management and shareholders depends on the market for corporate control — an interstate, indeed international, market that the State of Indiana is not authorized to opt out of, as in effect it has done in this statute." CTS App. at A26.

In the absence of any evidence as to the Control Share Chapter's effect on CTS Corporation and its shareholders, directors, officers and employees, the Seventh Circuit adopted the foregoing theory to prove that shareholders of

large Indiana corporations are unequivocally hurt by the Control Share Chapter. It is worth pointing out that the Seventh Circuit's theory is, in fact, just a theory. The Control Share Chapter provides a number of benefits for Indiana corporations, shareholders, directors, officers and employees, and to the extent the Court is not persuaded, by virtue of the divergent views of the eminent commentators on this point, the presumption that the Control Share Chapter is constitutional should apply. As for the alleged burdens brought about by the Control Share Chapter, the Seventh Circuit materially overstated the degree to which the Control Share Chapter is likely to affect tender offers without any specific analysis of its probable operation in practice.

A. The Control Share Chapter's Benefits Should not be Determined by the Seventh Circuit's Unsubstantiated Economic Theory.

In analyzing the Control Share Chapter, the Seventh Circuit followed the balancing test set out in *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).[8] In applying that test, the Seventh Circuit held that the legally cognizable interest of the State of Indiana — the welfare of Indiana residents — is not furthered by the Control Share Chapter and might even be hindered by it. CTS App. at A25. The Indiana Chamber and the Foundation are compelled to ask how, with no evidentiary record in this case and conflicting authority from the academic experts, the Seventh Circuit could so confidently make this assessment of the putative benefits to Indiana residents. Contrary to the Seventh Circuit, the Indiana Chamber and the Foundation believe that there are real and substantial benefits from the Control Share Chapter which flow to Indiana corporations

[8] CTS Corporation has taken the position that the Court should not even reach the *Pike* balancing test in holding that the Control Share Chapter does not violate the Commerce Clause. The *amici* agree, but assume, *arguendo*, for purposes of this brief, that the balancing test applies.

and their shareholders, officers and directors. Among those benefits are: First, the Control Share Chapter protects all shareholders by providing for shareholder approval of any change of control proposal, as in other similar corporate transactions. Second, the Control Share Chapter protects the minority shareholders by giving them dissenters' rights in the event a change of control is approved against their wishes. And, third, the Control Share Chapter promotes better corporate governance through the recruitment and retention of quality directors to govern Indiana corporations.[9] These benefits accrue to the advantage of the corporations, their employees, and the communities in which they are located.

[9] As is apparent from the remainder of the IBCL, the Indiana legislature was concerned with, among other things, protecting the quality of corporate governance in Indiana corporations by granting certain protections to corporate directors. (*See* note 7, *supra*, concerning the provisions of the IBCL dealing with directors' duties and liabilities.) It is well documented that the proliferation of actions against directors and the increased cost (and even unavailability) of director and officer liability insurance have led to a reluctance of individuals to serve as directors of publicly held corporations. *See, generally,* Bishop, *Law of Corporate Officers and Directors: Indemnification and Insurance;* Baum & Byrne, *The Job Nobody Wants: Outside Directors Find that the Risks and Hassles Just Aren't Worth It*, Bus. Wk., Sept. 8, 1986, at 56. It is a legitimate legislative concern that it is difficult for corporations to recruit and retain highly qualified individuals to serve as directors — particularly outside directors. The Control Share Chapter provides to shareholders the positive benefits of a control share acquisitions charter amendment without action by the directors that might be challenged as a breach of fiduciary duty. Similarly, the Control Share Chapter addresses the concern that the *absence* of employing defensive tactics in response to a hostile takeover might constitute a breach of fiduciary duty if it turns out that the terms of the offer were not in the best interests of the corporation or the shareholders. *See* Wander & LeCoque, *Boardroom Jitters: Corporate Control Transactions and Today's Business Judgment Rule*, 42 Bus. Lawyer 29, 49 (1986).

The benefits of the Control Share Chapter as understood by *amici* and the absence of such benefits in the view of the Seventh Circuit reveal the disparity of views on this subject. The magnitude of legal and business articles on the subject indicates that there is widely-held disagreement with respect to the benefits and burdens of takeovers.[10] As one commentator has put it, "[t]he debate has not gone on long enough for definitive solutions to a problem we are only beginning to understand. The empiric data is inadequate, and most important, there is no consensus on the goals we are trying to reach." Subak, *Takeovers: Where Are We? Where Do We Go?*, 41 Bus. Lawyer 1255, 1256 (August 1986). Into this climate of confusion and raging debate, the Seventh Circuit has attempted to inject certainty by simply

[10] *Compare* Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 Harv. L. Rev. 1161 (1981) (no resistance to tender offers by incumbent management can be justified), *with* Lowenstein, *Pruning Deadwood in Hostile Takeovers: A Proposal for Legislation*, 83 Colum. L. Rev. 249 (1983) (the advantages possessed by tender offerors under the current regulatory environment justify at least some obstructive tactics on the part of the incumbent board), *and* Bebchuk, *Toward Undistorted Choice and Equal Treatment in Corporate Takeovers*, 98 Harv. L. Rev. 1693 (1985) (neither unrestrained tender offers nor defensive tactics by management serve the best interests of corporate shareholders). *Compare* Ginsburg & Robinson, *The Case Against Federal Intervention in the Market for Corporate Control*, Brookings Review (Winter/Spring 1986) at 9 (the theory that the threat of tender offers forces management into a short-sighted strategy of maximizing current profits is incorrect), *with* Scherer, *Takeovers: Present and Future Dangers*, Brookings Review (Winter/Spring 1986) at 15 (takeovers have not resulted in improved post-takeover performance by acquired corporations). *Compare* Melloan, *New Debate Over Corporate Governance*, Wall St. J., Nov. 11, 1986, at 32, col. 3 (quoting those who argue that the threat of hostile tender offers makes incumbent management more responsive to the rights of shareholders), *with* Melloan, *The Backlash Against Corporate Raiders*, Wall St. J., Nov. 12, 1986, at 32, col. 3 (quoting a chief executive officer who argues that market competition forces efficient management and that the threat of hostile tender offers encourages excessive leveraging of assets).

saying that one argument is right and all the others are wrong.

In the absence of a resolution of the many issues surrounding tender offers by federal legislation, and in the absence of any evidence as to the benefits and the burdens of the Control Share Chapter, the presumption that state statutes in areas traditionally and properly regulated by the states are constitutional should be respected. *Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520, 524 (1959) ("If there are alternative ways of solving a problem, we do not sit to determine which of them is best suited to achieve a valid state objective. Policy decisions are for the state legislature, absent federal entry into the field"). Deferring to the policy decision of the State of Indiana would also promote one of the benefits of federalism — that states may act as laboratories for competing theories about governing. *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting); Ginsburg & Robinson, *The Case Against Federal Intervention in the Market for Corporate Control*, Brookings Review (Winter/Spring 1986) at 9, 14. Of course, the Commerce Clause is not subservient to this "laboratory" philosophy. However, when there is a genuine issue, as a matter of economic theory, as to whether legitimate state interests are furthered or hindered by a statute, the "laboratory" approach is appropriate.

In the final analysis, the State's policy decision will be tested in the marketplace. If the Control Share Chapter truly has the effect of decreasing shareholder wealth, in our free society shareholders will presumably be moved to invest in corporations chartered in states with different corporate laws. The market value of shares in publicly held Indiana corporations will decline, and growing Indiana businesses will have trouble going public. In short, if the Seventh Circuit's economic theory is correct and the Control Share Chapter operates in practice the way the Seventh Circuit speculated it would, Indiana businesses in general will pay the price. The *amici* do not share the Seventh Circuit's economic theory.

B. The Control Share Chapter is Far Less Burdensome to Tender Offerors Than the Seventh Circuit Believed.

The Seventh Circuit held that a state statute that effectively eliminates the possibility of tender offers succeeding, or of even being launched, is in mortal conflict with the Commerce Clause. The *amici* believe that a review of the actual operation of the Control Share Chapter will demonstrate that it does not set up a "gauntlet" that is incapable of being run.

Under the Control Share Chapter, if the shares acquired in a control share acquisition will put the acquiring person (a tender offeror or any other type of acquiror) over one of the three percentage control thresholds, the acquired shares will not have voting rights unless the shareholders of the target corporation approve a resolution reinstating voting rights for such shares. The issue of voting rights for the acquired shares will be determined at the next special or annual meeting of shareholders unless the acquiring person submits an acquiring person statement, in which case, if requested, the issue will be presented to a special meeting of the shareholders within 50 days of the request.

Several strategies for effectively conducting a tender offer for control, consistent with the Control Share Chapter, are evident. One option is simply to make a tender offer in compliance with the Williams Act for the number of shares the tender offeror desires to acquire, buy the shares, file an acquiring person statement, and begin a campaign to convince a majority of the shareholders to vote in favor of voting rights for the acquired shares. Nothing in the Control Share Chapter prohibits communicating with the shareholders prior to the vote. If unsuccessful in the shareholders' vote, the tender offeror will still own the acquired shares and will have all the rights with respect thereto, except voting rights. Furthermore, the tender offeror can sell his non-voting shares to one or more buyers, with full voting rights, provided no buyer exceeds a control threshold as a result of such purchase.

A more cautious option for the tender offeror would be to submit an acquiring person statement without launching a tender offer. After the date is set for the special shareholders' meeting, the tender offeror could solicit proxies to be used in voting on the voting rights issue or communicate in some other way with the shareholders. If the tender offeror wins the shareholder vote 50 days (or less) later, he can launch the tender offer.

Probably the option most likely to be used is for the tender offeror to simply launch a conditional tender offer. The terms of the tender offer would be that the tender offeror would purchase all tendered shares (up to the limit set forth in the offer), but only if a majority of the shareholders ultimately vote to reinstate the voting rights of the acquired shares. *See MacFadden Holdings, Inc. v. JB Acquisition Corp.*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 92,939 (2nd Cir. October 6, 1986) (holding that shares can be tendered pursuant to a tender offer conditioned upon certain regulatory approvals). The tender offeror's chances of winning the vote would be substantial, because those who have tendered their shares would have a financial interest in voting in favor of voting rights in the absence of an intervening higher offer. The tender offeror could further enhance his chances by soliciting proxies to be used at the special shareholders' meeting or by communicating in some other way with the shareholders. Obviously, if the tender offeror loses the shareholder vote, he loses the expenses of the tender offer, just as any unsuccessful tender offeror would, but he avoids becoming a substantial shareholder without commensurate voting rights.

CONCLUSION

Because the Control Share Chapter is not concerned with the buying and selling of shares in tender offers and is in the nature of a shareholder rights provision operative only *after* a control share acquisition, it is not preempted by the Williams Act. The *amici* believe the Control Share Chapter provides substantial benefits to Indiana constituencies with very little burden on tender offerors. The intense disagreement among those who have analyzed the issues in the tender offer debate should be resolved by the presumption of constitutionality of state statutes of this type, in the absence of evidence in this case and in the absence of action by Congress. The Seventh Circuit's holding that the Control Share Chapter is unconstitutional by virtue of the Supremacy Clause and the Commerce Clause should be reversed.

Respectfully submitted,

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(8) (6)

No. 86-71 & 86-97

IN THE
Supreme Court of the United States

OCTOBER TERM, 1986

CTS CORPORATION,

Appellant,

— vs. —

DYNAMICS CORPORATION OF AMERICA,

Appellee.

STATE OF INDIANA,

Intervenor-Appellant,

— vs. —

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

BRIEF *AMICUS CURIAE* OF THE STATE OF NEW YORK IN SUPPORT OF APPELLANTS

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INTEREST OF AMICUS CURIAE

Amicus, State of New York, by Robert Abrams, Attorney General of the State of New York, respectfully submits this brief in support of appellants pursuant to Supreme Court Rule 36.4. *Amicus* urges this Court to reverse the judgment of the court of appeals and to affirm the power of a state to enact legislation that adjusts the variety of interests effected by takeovers of local corporations.

New York has an interest in the issues presented by this appeal because this Court's decision may affect the validity of a recent amendment to the New York Business Corporation Law ("NYBCL"). The amendment, N.Y. BUS. CORP. LAW §912 (McKinney 1986), and the Indiana law challenged in this litigation, The Control Share Acquisitions Chapter of the Indiana Business Corporation Law, IND. CODE ANN. §§23-1-42-1 to 11 (Burns Cum. Supp. 1986), operate quite differently, but they advance common legitimate state interests. As *amicus*, New York seeks to protect those interests. New York emphasizes the power of states to enact legislation, consistent with *Edgar v. MITE Corp.*, 457 U.S. 624 (1982),[1] that apportions the local interests and rights affected by changes in corporate control and fundamental corporate events even though the legislation incidentally impacts on interstate commerce. The challenged Indiana act, Section 912 and numerous other state laws represent the best efforts of many states to exercise their traditional authority over such matters while complying with the limited guidelines articulated in *Edgar v. MITE, Corp.*

This Court's response to Indiana's attempt to prescribe rules governing the exercise of the voting rights associated with newly-acquired control shares may eventually guide lower courts' assessment of New York's statute. Like Indiana's law, Section 912 governs internal corporate matters; it does so by setting requirements for certain business combinations between New York

[1] The State of New York also participated as amicus curiae in *Edgar v. MITE Corp.*, and supported the constitutionality of the Illinois law challenged there.

resident domestic corporations and certain shareholders of 20 percent or more of the outstanding voting stock ("interested shareholders") of resident domestic corporations. Authority to regulate the voting rights of shares and prescribe requirements for business combinations traditionally has resided with the state under whose laws the corporation is organized. For example, section 912 restricts interested shareholders' access to corporate assets by prescribing requirements for mergers, consolidations, dissolutions and other dispositions of significant corporate assets. Its goal is to promote the long-term well-being of New York resident domestic corporations.

The type of business combination affected by section 912 usually accompanies highly-leveraged unilateral takeovers. These combinations frequently change the financial structure, character, investment and employment policies, and earnings of the local corporation. Too often such changes are initiated in order to fund the takeover itself and operate to the long-term detriment of the corporation. These combinations may also alter the legal relationships and expectations among and between shareholders of the resident domestic corporation. Interests outside the corporation may also be significantly affected, particularly those of suppliers and employees of the corporation and other local businesses. Choosing from several approaches, 32 states have enacted statutes that protect and balance the variety of interests implicated by transactions conceived to force major internal corporate changes in corporations deeply rooted in those states.[2]

Lastly, the State of New York is the home of thousands of corporations and corporate investors of every variety. The New York and American Stock Exchanges are located in New York and are pillars of the State's economy. As the site of a staggering volume of transactions involving corporate securities, assets and control, the State's interest in the Court's decision is

[2] Alaska, Arkansas, Delaware, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Hampshire, New Jersey, New York, Ohio, Oklahoma, Pennsylvania, South Carolina, South Dakota, Tennessee, Utah, Virginia, and Wisconsin.

keen: the decision may impact on the economy of the State, how people do business within it, and the development of its commercial law.

In sum, the State of New York has an interest in protecting the power of states to enact statutes which, by constitutionally permissible means, adjust the variety of local interests affected by corporate takeovers. We believe that the Indiana statute satisfies the requirements of the Commerce and Supremacy clauses. Likewise, we are satisfied that the New York statute is fully compatible with the provisions of the United States Constitution, although we recognize that the Court's decision in this case is not an occasion — and should not be the occasion — to resolve this question.

SUMMARY OF ARGUMENT

Acting pursuant to powers granted to it under the Supremacy and Commerce Clauses of the Constitution, Congress enacted the Williams Act, 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f)(1982), which brought a measure of protection to shareholders of corporations that were the targets of takeover efforts. In so doing, Congress did not evince an intention to preempt state statutes covering the same subject matter. It neither sought to impose a national governmental policy regarding corporate takeover contests nor to preclude the states from enacting laws that strike a different balance.

Recently, in *Edgar v. MITE Corp.* this Court considered the effect of the Williams Act on an Illinois statute which regulated certain takeover contests and declined to hold that the Williams Act preempts state regulation in this area or otherwise imposes an overriding national policy respecting takeovers. Nevertheless, the court of appeals devined the existence of such a policy and invalidated the Indiana statute which sought to regulate the exercise of voting rights in connection with takeovers of corporations having substantial contacts with that state. In so doing, the lower court cast grave doubt on the traditional power of a state to enact legislation that affects transactions designed to capture corporate control, alter corporate governance and

reallocate substantial assets of corporations firmly connected to that state. Its decision should be reversed.

Absent express preemption of state power by Congress, a federal law preempts only state laws that cannot be reconciled with it. The purpose and scope of the Williams Act are limited to protecting shareholders through full and fair disclosure of information pertinent to securities transactions. State laws that provide other benefits to shareholders, regulate local corporations, accord rights to their employees and aid the surrounding economies are not affected by the Williams Act. Rather than regulating the purchase and sale of securities, such laws usually operate to limit an individual's exercise of control over a corporation or his ability to reallocate significant corprate assets. Misconstruing the reach of the Williams Act, the courts below erroneously struck down the Indiana act even though the purposes and provisions of the two statutes do not conflict and could easily have been reconciled. Contrary to the holdings of the courts below, the Indiana act need not cause any delay that conflicts with the provisions of the Williams Act.

The Commerce Clause itself imposes restraints on the power of states to enact laws that directly burden interstate commerce or discriminate against it. This Court has consistently acknowledged the authority of the several states to implement nondiscriminatory laws that are intended to carry out legitimate state purposes.

The corporation is a creature of state law and regulation of the internal affairs of resident corporations is manifestly a legitimate state concern. In striking down the Indiana act on Commerce Clause grounds, the court of appeals accorded only lip service to Indiana's substantial concern in apportioning rights affected by changes in control and asset deployment of corporations that incorporate in Indiana and otherwise are strongly tied to the state. The interests of states in those internal corporate matters are legitimate and substantial, and if a state statute is drawn to further them it should withstand challenges based on the Commerce Clause.

Indiana's statute is constitutional because it only regulates post-acquisition voting rights for control share acquisitions. It does not directly regulate interstate transactions; nor does it discriminate against acquisitions commenced by out-of-state residents. Despite the holdings of the courts below, the extent of the Indiana statute's burden on interstate commerce is speculative. The record contains no evidence that the statute will adversely affect interstate commerce. On the other hand, the Indiana act benefits local shareholders by granting them a voice in proposed material changes in voting control, permitting them to consider a tender offer without fear of a shareholder stampede, and promoting fair treatment of non-tendering shareholders.

The Indiana act is only one of a variety of measures enacted by states that bear on the subject of corporate takeovers. The constitutionality of each such measure should be assessed individually given differences in the degree of local contact required, the particular state interest intended to be addressed and other factors. The court of appeals' decision appears to have a broad sweep. It draws into question any state law which a court may view as slowing "the important commerce of corporate control," *see Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 264 (7th Cir. 1986). This Court should reject the lower court's effort to override state laws and impose a national policy without the benefit of clear Congressional guidance.

ARGUMENT

I. The Preemption Holding Of The Courts Below Finds Little Support In The Williams Act Or *Edgar v. MITE Corp.*, And Unnecessarily Casts Doubt On State Laws That Do Not Conflict With The Williams Act

Absent explicit preemptive language in a federal statute, courts should not declare a state statute invalid under the Supremacy Clause, U.S. Const. art. VI, cl.2, unless the federal and state laws are irreconcilable. *Hillsborough County, Florida v. Automated Medical Laboratories, Inc.*, 471 U.S. 707 (1985); *Pacific Gas & Electric Co. v. State Energy Resources Conservation and Development Commission*, 461 U.S. 190 (1983); *see Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977). The preemption analysis starts with the assumption that in fields traditionally occupied by the states, "the historic police powers of the States were not to be superceded by the Federal Act unless that was the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947). *See City of Burbank v. Lockheed Air Terminal Inc.*, 411 U.S. 624, 643 (1973) (Rehnquist, J., dissenting).

Aside from express preemptive language, the clear and manifest purpose of Congress to preempt all state law may be found where: the nature of the subject matter regulated permits no other conclusion, *Florida Lime and Avocado Growers, Inc. v. Paul*, 373 U.S. 132 (1963); a pervasive scheme of federal regulation leaves no room for supplementary state regulation, *City of Burbank v. Lockheed Air Terminal Inc.*, 411 U.S. at 633; "compliance with both federal and state regulations is a physical impossibility," *Florida Lime and Avocado Growers, Inc. v. Paul*, 373 U.S. at 142-43; or state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Edgar v. MITE Corp.*, 457 U.S. at 631 quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941).

States have traditionally occupied the field of corporate law. *Burks v. Lasker*, 441 U.S. 471, 479-80 (1979). "Corporations are creatures of state law, and ... state law will govern the internal affairs of the corporation." *Cort v. Ash*, 422 U.S. 66, 84 (1975); *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 478-79 (1977). In this appeal, the presumption against preemption is entitled to great weight due to the absence of any contentions that the Williams Act contains express preemptive language, evinces an intent to occupy the entire field or that it would be impossible to comply with the provisions of the Williams Act and the significantly different provisions of the Indiana law. *See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware*, 414 U.S. 117, 127 (1973). Here, as in *Edgar v. MITE Corp.*, the sole issue is whether the Indiana law frustrates the objectives of the Williams Act in "some substantial way." *Edgar v. MITE Corp.*, 457 U.S. at 632 (White, J.).

Resolution of this issue requires that operation of the challenged state law be measured against the purpose of the federal statute. The Williams Act, passed in 1968, sought to close the regulatory gap caused by the increased use of cash tender offers in corporate acquisitions, "a device that had 'removed a substantial number of corporate control contests from the reach of existing disclosure requirements of the federal securities law.' " *Edgar v. MITE Corp.*, 457 U.S. at 632, quoting *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 22 (1977). The Williams Act is primarily a full disclosure law which furnishes important information to all target shareholders, and provides certain protections to target shareholders who elect to tender their stock.[3]

[3] Under the Williams Act, disclosure is required of persons who acquire more than five percent of certain classes of securities or commence a tender offer which would give them ownership of more than five percent of certain classes of securities. 15 U.S.C. §§78m(d)(1), 78n(d)(1). The information that must be disclosed includes: the background and identity of the acquiror; the source of the funds to be used in making the purchase; the purpose of the purchase, including any plans to liquidate the company or make major changes in corporate structure; and the extent of the acquiror's holdings in the target

(Footnote continued)

When Congress amended the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. §§78a *et seq.* by enacting the Williams Act, the amendment did not disturb section 28(a) of the 1934 Act, 15 U.S.C. §78bb(a). In pertinent part, Section 28(a) provides as follows:

> Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations thereunder.

Section 28(a) clearly expresses Congress' intent to limit the preemptive effect of the federal securities laws. This intent is grafted onto the Williams Act. Thus, any inquiry into the preemptive effect of the Williams Act must be illuminated by the unmistakeable fact that section 28(a) is intended to "protect, rather than limit, state authority." *Leroy v. Great Western United Corp.* 443 U.S. 173, 182 (1979); *see Agency-Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029, 1038 (1st Cir. 1982).

The Indiana control share acquisitions law does not conflict with the Williams Act or frustrate its objectives in a substantial way. The statutes operate in related, but separate arenas. The Indiana law defines the post-acquisition voting rights of certain controlling shares while the sole purpose of the Williams Act is to provide investors with full and fair disclosure regarding tender offers. *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. at 35; *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 58

(Footnote continued)
company. 15 U.S.C. §78m(d)(1). With respect to tender offers: (1) stockholders who tender their shares may withdraw them during the first 7 days of a tender offer and if the offeror has not yet purchased their shares, at any time after 60 days from the commencement of the offer, 15 U.S.C. §78n(d)(5); and (2) all shares tendered must be purchased for the same price; if an offering price is increased, those who have already tendered receive the benefit of the increase. 15 U.S.C. §78n(d)(7). *See Edgar v. MITE Corp.*, 457 U.S. at 632.

(1975); 113 Cong. Rec. 24664 (1967)(Comments of sponsor, Senator Williams); S. Rep. No. 550, 90th Cong., 1st Sess. (1967)(Senate Report). Moreover, the Indiana law protects a broader range of interests than those protected by the Williams Act, including local economic and social interests likely to be affected by transfers of corporate control. *See Edgar v. MITE Corp.*, 457 U.S. at 647 (Powell, J., concurring in part).

The court of appeals swept aside the Indiana law on the ground that it frustrated an objective of the Williams Act — the "delicate balance" struck between the tender offeror and incumbent management. *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 262 (7th Cir. 1986). However, in *Piper v. Chris-Craft Industries, Inc.*, this Court stated:

> Congress was indeed committed to a policy of neutrality in contests of control, but its policy of evenhandedness does not go to either the purpose of the legislation or to whether a private cause of action is implicit in the statute. Neutrality, is, rather, but one characteristic of legislation directed toward a different purpose— the protection of investors.

430 U.S. at 29. Moreover, in *Edgar v. MITE Corp.*, Justice White's conclusion that the policy of neutrality underlying the Williams Act should be accorded preemptive effect failed to command a majority of this Court.[4] *See Edgar v. MITE Corp.*, 457 U.S. at 646 (Powell, J., concurring); *Id.* at 655 (Stevens, J., concurring). In brief, the decision to strike down the Indiana act was supported neither by this Court's case law nor the

[4] Justice White's opinion has been accorded great weight by several courts of appeals, *Fleet Aerospace Corp. v. Holderman*, 796 F.2d 135 (6th Cir. 1986); *Securities and Exchange Commission v. Carter Hawley Hale Stores, Inc.*, 760 F.2d 945 (9th Cir. 1985); *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d 558 (6th Cir. 1982); *National City Lines, Inc. v. LLC Corp.*, 687 F.2d 1122 (8th Cir. 1982), but none of the statutes reviewed by those courts was anologous to Indiana's law.

legislative history of the Williams Act. Tacitly conceding that it had found no clear and manifest intent of Congress to preempt state laws like the one challenged here, the court of appeals nevertheless took the required "big leap," and toppled the Indiana law. *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d at 262.

The court of appeals' "delicate balance" analysis also casts doubt on a variety of other state statutes which *amicus* believes do not frustrate the full and fair disclosure purpose of the Williams Act or upset that act's policy of neutrality. Generally, these statutes protect interests far broader than those addressed in the Williams Act. These statutes reflect a variety of approaches. Control share acquisitions statutes, like that of Indiana, allow shareholders or their duly elected directors to determine voting rights for control share acquisitions. Business combination statutes generally require similar approval for business combinations, broadly defined to include a wide range of transactions involving substantial corporate assets.[5] Fair value statutes grant non-tendering minority shareholders the right to receive a statutorily prescribed fair price to protect them from being "freezed out" by the controlling shares.[6] Still other statutes combine features of each of the above laws.[7] The delicate balance reasoning adopted by the court of appeals implies that it would invalidate all of these statutes because they may make acquisition of control of a corporation or access to its assets more

[5] New York, N.Y. BUS. CORP. LAW §912 (McKinney 1986), New Jersey, 1986 N.J. Sess. Law Serv. Chap. 74 (West), and Kentucky, KY. REV. STAT. §271A.397 (1984) have enacted different versions of business combination statutes.

[6] Pennsylvania, PA. STAT. ANN. tit. 15, §1910 (Purdon Supp. 1986), has enacted a fair value statute.

[7] Hybrid statutes have been enacted by Wisconsin, WIS. STAT. §§180.25(9), 180.725 (1986); Maryland, MD. CORPS. & ASS'NS CODE ANN. §§3-601 *et seq.* (1985); Kentucky, KY. REV. STAT. §271A.397-99 (1984); Michigan, MICH. COMP. LAWS §§450.177 *et seq.* (Supp. 1986); and other states.

difficult to accomplish.[8] As demonstrated earlier, the Williams Act should not be construed to have such an intrusive impact on traditional state authority.

In sum, read in light of settled principles of federalism, section 28(a) of the 1934 Act, the legislative history of the Williams Act and the broad traditional role of the states in regulating corporations, no basis exists for concluding that Congress intended to preempt state laws pertaining to the exercise of voting rights, use of corporate assets, transfer of corporate control or treatment of minority interest shareholders. All of these transactions impact on internal corporate matters and implicate interests beyond those sought to be protected by the Williams Act.

In addition, no policy or objective of the Williams Act is frustrated by these state laws. Lower court decisions that find preemption appear to be based upon the mistaken belief that since interstate securities transactions are used to accomplish these major corporate changes, no state can enact legislation which affects these transactions. *Cf. Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 127 (1978) (Court rejected the "novel suggestion that because the economic market for petroleum products is nationwide, no state has the power to regulate the retail marketing of gas.") But Congress has not addressed the impact of these major corporate changes, and until it does so, this Court should leave the states free to serve as laboratories for finding effective ways of regulating takeovers. Accordingly, thi.

[8] The business combinations regulated by Section 912, including mergers, consolidations, dissolutions and other reallocations of substantial corporate assets, have long been regulated by New York law in some fashion. Measuring section 912 against the Williams Act reveals that it *does not*: interfere with the disclosure requirements of the Williams Act; purport to regulate the purchase and sale of securities; impose time limits inconsistent with the Williams Act (§912(b)); effect voting rights; restrict the acquiror's ability to oust incumbent management; or permit a state official to usurp shareholders' decisions to sell their shares. The New York act only restricts the freedom of resident domestic corporations to execute a business combination that will redirect substantial corporate assets principally for the benefit of the newly-acquired controlling interest.

Court should hold that Indiana's control share acquisitions statute is not preempted by the Williams Act. *See Hillsborough County, Florida v. Automated Medical Laboratories, Inc.; Pacific Gas & Electric Co. v. State Energy Resources Conservation and Development Commission.*

II. State Statutes, Like Indiana's, That Adjust The Various Interests Effected By Corporate Takeovers Are Constitutional For They Are Nondiscriminatory And Have Only Incidental Effects On Interstate Commerce

The Commerce Clause provides that "Congress shall have Power... to regulate Commerce... among the several States." U.S. Const. art I, §8, cl. 3. While it is well settled that the dormant Commerce Clause is a limitation on the power of the states to affect interstate commerce, *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299 (1852), it is also clear that states are not precluded from enforcing local laws that incidentally burden interstate commerce. *Lewis v. B.T. Investment Managers, Inc.*, 447 U.S. 27 (1980); *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456 (1961). Direct burdens on interstate commerce are prohibited, but the Commerce Clause permits states to implement laws which affect interstate commerce if the state interest is legitimate, and the state regulation is nondiscriminatory. *Brown-Forman Distillers Corp. v. New York State Liquor Authority ("NYSLA")*, 106 S. Ct. 2080 (1986); *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970).

Minimal inquiry is required to recognize the constitutional infirmity in state statutes that directly regulate or discriminate against interstate commerce. *See, e.g., Brown-Forman Distillers Corp. v. NYSLA*, 106 S. Ct. at 2080; *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978). In contrast, when a state statute has only indirect effects on interstate commerce and regulates evenhandedly, courts must examine whether the state's interest is legitimate and whether the burden on commerce is outweighed by the local benefits. *Brown-Forman Distillers Corp. v. NYSLA*, 106 S. Ct. at 2080; *Edgar v. MITE Corp.*, 457 U.S. at 640; *Pike v. Bruce Church, Inc.*, 397 U.S. at 142. Where, as here, the challenged state statute furthers weighty, legitimate state interests it does not offend the constitution.

Citing *Edgar v. MITE Corp.*, the courts below held that Indiana's control share acquisitions statute violated the Commerce Clause. However, the majority opinion in *Edgar v. MITE Corp.* supports neither the holding nor reasoning of the courts below. First, the characteristics of the Indiana control share acquisitions statute bear no resemblance to the provisions of the Illinois Business Takeover Act which this Court invalidated.[9] Furthermore, the Court acknowledged the legitimacy of Illinois' interest in protecting local investors, but concluded that the means used unnecessarily burdened interstate commerce and did not plainly further the interests asserted by Illinois. *Id.* at 643-46. Ignoring the limited reach of this Court's holding in *Edgar v. MITE Corp.*, the courts below invalidated the Indiana law without giving proper weight to the legitimate interests of Indiana or the variety of benefits derived from its statute. In fact, the court of appeals went so far as to suggest that generally states have limited interests in regulating the effects of corporate takeovers. Of course, several weighty interests support state legislation that adjusts the variety of local interests likely to be directly effected by corporate takeovers. Note, *State Regulation of Tender Offers: Legislating Within The Constitutional Framework*, 54 Fordham L. Rev. 885, 901 (1986). Takeovers are designed to have a direct impact on the fundamental internal affairs of target corporations, specifically corporate control and the allocation of assets. For example, they implicate interests of employees, minority shareholders and incumbent management as well as businesses located in the area where the corporation does substantial business. Thus, while takeovers may be accomplished by interstate transactions, local interests traditionally regulated by the states are frequently impacted directly.

[9] The Illinois act allowed the Illinois Secretary of State to block indefinitely a nationwide tender offer. The Indiana act, on the other hand, assigns no role to the state in takeover contests, and does not regulate the transfer of stock.

Corporations and corporate shares are creatures of state law. *Cort v. Ash*, 422 U.S. at 84. Despite increased trading of corporate shares in interstate and international commerce, shares remain items over which the states have significant authority. The initial features of corporate stock, including voting rights, were created by states, and states retain the authority to modify or amend those features. That authority includes the power to define the circumstances under which shares may be used to gain control over a corporation or to reallocate corporate assets. Thus, contrary to the court of appeals' belief, the federal government and states share a joint interest in the "commerce of corporate control." *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d at 264.

Some of the specific goals states seek to achieve by enacting various forms of takeover legislation include: (1) protecting local non-tendering shareholders from the effects of two-tier "freeze-out" transactions; (2) permitting shareholders to participate in decisions regarding fundamental corporate events such as mergers, consolidations, and sales and pledges of assets; (3) encouraging certain types of investment strategies considered good for the economy of the state; and (4) eliminating the need for incumbent management to focus upon certain defensive strategies considered unhealthy for the state's economy. Each of these interests is important to the states and in assessing the validity of a state statute under the Commerce Clause, courts should accord these interests great weight.

The court of appeals' failure to accord proper weight to Indiana's stated interests renders its *Pike* analysis defective.[10] Unlike the statute considered in *Edgar v. MITE Corp.*, Indiana has a strong interest in the corporations covered by its control share acquisitions act. The Indiana act applies only to corporations organized under the laws of Indiana with 100 or more

[10] Application of the *Pike* balancing test is appropriate because the Indiana act does not directly regulate interstate transactions. Instead, once the stock acquisition is completed, the statute allows shareholders to determine whether voting rights will be accorded to an acquiror of a controlling interest.

shareholders which have their principal place of business, principal offices or substantial assets within Indiana, and more than ten percent of their shares owned by Indiana residents. Thus, the Indiana act covers corporations that were incorporated in the state and in which Indiana residents have a substantial ownership interest and which do substantial business in the state or maintain substantial assets there.

These firm ties between the covered corporations and Indiana permit the state to pursue several permissible objectives: protecting resident shareholders and local economies, and regulating internal corporate affairs. Sargent, *Do The Second Generation State Takeover Statutes Violate The Commerce Clause?*, 8 Corp. L. Rev. 3 (1985). Because the Indiana law is directed at local matters, its effect on interstate commerce is incidental and its burden on interstate commerce is modest. Additionally, the Indiana law regulates evenhandedly inasmuch as it makes no distinction between acquisitions initiated by out-of-state residents and those initiated by state residents.

The Indiana law advances the legitimate state interests identified. It benefits Indiana shareholders because it only applies to Indiana corporations in which Indiana residents have a substantial ownership interest. It protects shareholders by permitting a majority of disinterested shareholders to determine whether a material change in voting control is in their best interests. Because it requires express shareholder approval of a transfer of controlling voting rights in a corporation, the statute allows resident shareholders to discount the possibility of a shareholder stampede and permits them to focus on factors, including the probable local economic and social impact of a takeover, which they might not otherwise evaluate.

The Indiana act also advances the state's interest in regulating the internal affairs of corporations organized under the laws of Indiana. The statute is drawn to further this interest. It applies to voting rights, manifestly an internal matter, of corporations organized under the laws of Indiana. *APL Limited Partnership v. Van Dusen Air, Inc.*, 622 F. Supp. 1216, 1223 (D.C.

Minn. 1985). It does not apply to foreign corporations as did the statute examined in *Edgar v. MITE Corp.*

We are especially troubled by the aspect of the court of appeals' opinion that suggests that the Commerce Clause condemns state statutes that require shareholder or board of director approval of fundamental internal corporate changes initiated through interstate stock transactions. This notion implicates statutes like the one enacted by New York even though they plainly advance legitimate state interests without excessively burdening interstate commerce.

In this regard, Section 912, furthers several legitimate state interests. As a threshhold matter, the "resident domestic corporations" covered by section 912 are closely connected to New York so as to achieve the State's permissible purposes.[11] Secondly, Section 912 furthers several important state objectives, chief among them is promoting the long-term well-being of New York resident domestic corporations. *See* Governor's Program Memorandum, 1985 N.Y. Laws Chap. 915. The New York law accomplishes this goal by forbidding resident domestic corporations from engaging in business combinations with an interested shareholder for five years unless the business combination or controlling share acquisition was approved by the board of directors prior to the interested shareholder's stock acquisition date. Section §912(b). Five or more years after the interested shareholder's stock acquisition date, the resident domestic corporation may engage in a business combination with the interested shareholder if it obtains the affirmative vote of the holders of a majority of the outstanding stock not beneficially owned by such interested shareholder or pays the shareholders, other than the interested shareholder, a statutorily prescribed formula price designed to ensure that all holders of shares of

[11] The jurisdictional predicate required to trigger Section 912 is more strict than under Indiana law. Section 912 only covers corporations organized under the laws of New York *and* which have (1) their principal offices *and* (2) significant business operations *and* (3) at least 10 percent of the ownership of its voting stock located in New York. NYBCL §912(a)(13).

voting stock will receive at least the highest price per share paid by the interested shareholder, determined as of the date such business combination was first proposed in its final, definitive form. NYBCL §912(c).[12]

Thus, section 912 has the following effects: (1) it encourages takeovers that the acquiror and target management agree are in the best interests of New York corporations, their employees and shareholders; (2) it discourages unilateral takeovers which depend on immediate access to significant assets of the corporation; (3) it encourages long-term investment commitment by interested shareholders who acquired their controlling interest without the approval of the board of directors; and (4) it protects resident non-tendering shareholders from "freeze-out" transactions.[13] Achieving each of these benefits is important to the economic and social well-being of New York.

On the other side of the scale, section 912 does not excessively burden interstate commerce. It has a limited impact on the interstate commerce of corporate stock and control. In contrast to the statutes struck down in *Edgar v. MITE Corp.*, and by various other federal courts, section 912 does *not*: (1) regulate the sale of shares; (2) protect incumbent management from replacement by an interested shareholder; (3) limit the voting rights of newly-acquired shares; (4) require approval of the acquisition of controlling interests; (5) prohibit a change of the corporation's line of business; (6) grant the State a role in determining whether an interstate acquisition will proceed; or (7) deprive shareholders of the right to sell their shares at a premium.

[12] A related provision of New York law, NYBCL §513, restricts the use of "greenmail" by resident domestic corporations by requiring board of director and shareholder approval of such purchase or agreement to purchase.

[13] Two corollary benefits are discouraging excessive corporate debt and encouraging long-term interests, especially research and development and business diversification.

The court of appeals' opinion nonetheless calls statutes like Section 912 into question apparently on the ground that the Commerce Clause bars states from sanctioning any activity that slows "the important commerce in corporate control." *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d at 264. Implicit in the court's opinion is its belief that tender offers benefit shareholders and, therefore, the Commerce Clause should protect tender offers. In other words, under the guise of a Commerce Clause analysis, the court of appeals imposed its economic judgment regarding the value of tender offers. Such economic policy judgments, however, are reserved for the Congress or state legislatures. In the absence of a national policy regarding corporate takeovers, it is not appropriate for federal courts to attempt to fill the void by judicial interpretations of the Commerce Clause. This is especially so in light of Congress' disinclination, to date, to formulate an approach to the issue and the disputed economic data regarding the value of takeovers, particularly highly-leveraged hostile ones. Coffee, *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role In Corporate Governance*, 84 Col. L. Rev. 1145 (1984); *see* Tushnet, *Rethinking the Dormant Commerce Clause*, 1979 Wisc. L. Rev. 125, 156; Lipton, *Takeover Bids in the Target's Board Room*, 35 Bus. Law. 101 (1979).

CONCLUSION

For all the foregoing reasons, the decision below should be reversed.

Dated: New York, New York
December 4, 1986

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AMICUS CURIAE

BRIEF

(9) (7)

Nos. 86-71 & 86-97

IN THE

Supreme Court of the United States

October Term, 1986

CTS CORPORATION,

Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

STATE OF INDIANA,

Intervenor-Appellant,

v.

DYNAMICS CORPORATION OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

AMICUS CURIAE BRIEF OF STATE OF MINNESOTA

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AMICUS CURIAE BRIEF OF STATE OF MINNESOTA

INTEREST OF AMICUS CURIAE

Amicus Curiae State of Minnesota, through its Attorney General Hubert H. Humphrey, III (hereinafter "Minnesota"), respectfully submits this brief in support of the appellants. Resolution of the issues involved in this appeal will have a profound impact on Minnesota for two principal reasons.

First, this case raises a significant question regarding a state's authority to regulate the internal affairs of domestic corporations. The states' historical and longstanding authority to enact business corporation laws, without regard to the residency of the corporation's shareholders, has been severely undermined by the decision now under review by the Court. Consequently, Minnesota and its body of corporate laws,[1] which apply to corporations by reason of their incorporation in Minnesota without shareholder residency requirements, can be tremendously affected by the decision in this case.

Second, Minnesota has promulgated its own Control Share Acquisition Act (hereinafter "MCSAA").[2] It was enacted by the Minnesota Legislature in 1984 as part of an extensive modification of Minnesota's corporate takeover statutes, with an express purpose of conforming Minnesota law to this Court's decision in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982).[3] The 1984 Minnesota corporate takeover legislation is comprised of two different parts: (a) a major revision of Minn. Stat. ch. 80B ("Chapter 80B"), the state securities law which regulates the registration of tender offers, and (b) the MCSAA, which consists of amendments to Minn. Stat. ch. 302A, the Minnesota Business Corporation Act, and requires shareholder approval of "control share acquisitions," includ-

[1] Minn. Stat. ch. 302A (1984), as amended.

[2] Minn. Stat. § 302A.671 (Supp. 1985) as amended by Act of March 24, 1986, ch. 431, §§ 2 and 21, 1986 Minn. Laws 703, 706; the proxy provision relating thereto, Minn. Stat. § 302A.449, subd. 7 (Supp. 1985) as amended by Act of March 24, 1986, ch. 431, § 1, 1986 Minn. Laws 703; and the relevant definitional provisions, Minn. Stat. § 302A.011, subds. 37-41 (1984 & Supp. 1985). These statutory provisions are contained in the Appendix to this brief.

[3] Act of April 25, 1984, ch. 488, § 1, subd. 2(4), 1984 Minn. Laws 471.

ing those effected through tender offers.[4] The MCSAA was amended in both the 1985 and 1986 Minnesota legislative sessions.[5]

In November, 1984, the Eighth Circuit Court of Appeals concluded that Chapter 80B is constitutional. *Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906 (8th Cir. 1984). However, just recently, the Minnesota United States District Court determined that the MCSAA was unconstitutional as violating the Commerce and Supremacy Clauses of the United States Constitution, and that decision is now on appeal to the Eighth Circuit Court of Appeals. *Gelco Corp. v. Coniston Partners*, Civ. No. 3-86-847 (D. Minn. filed Nov. 7 and 10, 1986), *appeal docketed*, No. 86-5418 (8th Cir. filed Nov. 10, 1986).[6]

[4] Act of April 25, 1984, ch. 488, 1984 Minn. Laws 470.

[5] Act of June 24, 1985, 1st Spec. Sess. ch. 5, 1985 Minn. Laws 1630, and Act of March 24, 1986, ch. 431, §§ 1, 2 and 21, 1986 Minn. Laws 703, 706.

[6] The constitutionality of the MCSAA has been the subject of two prior cases. In *Edudata Corp. v. Scientific Computers, Inc.*, 599 Supp. 1084 (D. Minn.), *appeal dismissed*, 746 F.2d 429, 430 (8th Cir. 1984), the court denied an acquiring person's motion for a temporary restraining order with respect to enforcement of the Minnesota legislation. 599 F. Supp. at 1086, 1088. Thereafter, the case was settled by the offering and target companies and thus no final decision was rendered by the court. A further challenge in *APL Limited Partnership v. Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985), *vacated*, Civil No. 4-85-932 (Dec. 18, 1985), resulted in a decision that the MCSAA, as amended by the 1985 Minnesota Legislature, violated the Commerce Clause of the United States Constitution. *Id.* at 1220-25. This decision was appealed to the Eighth Circuit Court of Appeals, which heard the appeal on an expedited basis but ultimately was forced to dismiss the appeal as moot when the offeror and target company settled. Order, Nos. 85-5285, 85-5286 (8th Cir., Jan. 7, 1986). However, prior to dismissing the appeal, the Eighth Circuit directed the district court to vacate its decision and refused to actually dismiss the appeal or dissolve the stays pending appeal until it received the district court vacation order. Order, Nos. 85-5285, 85-5286 (8th Cir., Nov. 26, 1985).

The MCSAA is substantially similar to, but in some material respects different from, the Indiana Control Share Acquisition Act (hereinafter "ICSAA") under review in this case. The most significant difference between the two laws is that the shareholder vote under the MCSAA must be completed within twenty (20) business days of the target company's receipt of the required information,[7] which coincides precisely with the minimum offering period under the Williams Act,[8] whereas the corresponding provision under the ICSAA is fifty (50) calendar days.[9] Although some differences exist between the MCSAA and ICSAA, resolution of the instant appeal will likely impact the constitutionality of the MCSAA.

For the reasons expressed herein, Minnesota has a distinct, concrete and substantial interest in this appeal.

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[7] Act of March 24, 1986, ch. 431, § 2, 1986 Minn. Laws 703.

[8] 17 C.F.R. § 240.14e-1 (1986).

[9] Ind. Code Ann. § 23-1-42-7 (Burns Cum. Supp. 1986). Other differences between the Indiana and Minnesota laws include: (1) the ICSAA requires shareholder approval to determine whether the acquiring person may have voting rights, Ind. Code Ann. § 23-1-42-9 (Burns Cum. Supp. 1986), and the MCSAA provides for shareholder approval prior to consummation of the control share acquisition, Minn. Stat. § 302A.671, subd. 4 (Supp. 1985); (2) shareholder approval under the ICSAA requires a majority of "disinterested" shareholders, Ind. Code Ann. § 23-1-42-9 (Burns Cum. Supp. 1986) while the MCSAA provides for the majority vote of all shareholders, Minn. Stat. § 302A.671, subd. 4(a)(1) (Supp. 1985); and (3) the ICSAA requires the acquiring person to pay the expenses of the shareholder vote, Ind. Code Ann. § 23-1-42-7 (Burns Cum. Supp. 1986), whereas there is no such provision in the MCSAA.

SUMMARY OF ARGUMENT

The court of appeals decision is inconsistent with well-recognized principles relating to the states' authority to enact corporate laws. In accordance with the states' power to adopt business corporation statutes, control share acquisition laws, like the ICSAA and MCSAA, are valid and constitutional enactments. They neither violate the Commerce Clause nor the Supremacy Clause of the United States Constitution.

As to the Commerce Clause assertions, control share acquisition legislation does not directly burden interstate commerce because these business corporation statutes apply only when the target company is incorporated under the law of the regulating state. The presence of this long-accepted nexus for state corporate law regulation—state of incorporation—dispels any claims that control share acquisition legislation is *per se* invalid as a direct burden on interstate commerce.

In addition, any indirect burdens occasioned by control share acquisition laws do not clearly exceed the benefits underlying the statutes. The state benefits are substantial in extending the doctrine of shareholder democracy to a target company's shareholders, thereby allowing shareholders to decide the destiny of their company; mitigating the coercive nature of control share acquisitions; inhibiting the abusive use of takeover tactics by both target and offering companies; and enhancing a state's business environment. In relation to these benefits, the legislation imposes an insubstantial burden on interstate commerce which is identical to the burden imposed by reason of a shareholder vote on a merger proposal. Of course, mergers have historically and constitutionally been subject to the shareholder approval process.

The Supremacy Clause claims are similarly without merit. The control share acquisition statutes are consistent with the

Williams Act in that the objective of the laws, shareholder protection, is identical; time frames for the shareholder vote under the ICSAA, and certainly under control share acquisition laws like the MCSAA, do not conflict with the timing provisions of the Williams Act; and the state legislation is not contrary to the Williams Act regulation of non-tender offer control share acquisitions.

The decision of the court of appeals should be reversed.

ARGUMENT

I. CONTROL SHARE ACQUISITION LEGISLATION, LIKE THE ICSAA AND MCSAA, DOES NOT VIOLATE THE COMMERCE CLAUSE.

A. Background.

Control share acquisition legislation, such as the ICSAA and MCSAA, was adopted pursuant to the states' longstanding and unquestioned authority to regulate the internal affairs of businesses incorporated within their respective jurisdictions. *See, e.g., Burks v. Lasker*, 441 U.S. 471, 478 (1979); *Cort v. Ash*, 422 U.S. 66, 84 (1975); *Ashley v. Ryan*, 153 U.S. 436, 446 (1894). In accordance with this historical power, state corporate laws have traditionally governed a multitude of matters affecting domestic companies and their shareholders. For example, state corporate laws have always provided various rights and protections to domestic company shareholders, whether or not the shareholders reside in that particular state,[10] including procedures for shareholders collectively to

[10] *See, e.g.*, Minn. Stat. §§ 302A.405 (1984) (consideration for shares); 302A.413 (1984) (preemptive rights); 302A.467 (1984) (shareholder remedies); 302A.471 (1984) (rights of dissenting shareholders).

decide matters which have a major impact on the corporation.[11]

As a rational extension of existing corporate law, the control share acquisition provisions afford to shareholders a valuable right in the form of an opportunity to determine as a group whether they desire a change in control of their corporation—a change that can have a dramatic impact on the company. In providing this statutory right, the state legislatures have granted shareholders of their domestic corporations the same kind of voting control that those shareholders have traditionally exercised over other forms of transactions which can also have a substantial impact on a domestic corporation, *i.e.*, mergers, exchanges of shares, and the sale of all or substantially all of the corporation's assets. *See, e.g.*, Minn. Stat. §§ 302A.601-302A.661 (1984).

The ICSAA, and similar laws like the MCSAA, constitutes a unique, innovative and proper approach in furthering the fundamental concept of shareholder democracy. This form of legislation has been the subject of scholarly comment which concludes that the legislation is constitutional.[12]

[11] *See, e.g.*, Minn. Stat. §§ 302A.601 - 302A.661 (1984) (shareholder approval of mergers, exchanges of shares, and the sale of all or substantially all of the company's assets).

[12] *See* Johnson, *Minnesota's Control Share Acquisition Statute and the Need for New Judicial Analysis of State Takeover Legislation*, 12 Wm. Mitchell L. Rev. 183 (1986); Profusek and Gompf, *State Takeover Legislation After MITE: Standing Pat, Blue Sky, or Corporation Law Concepts*, 7 Corp. L. Rev. 3, 27-41 (1984); Note, *Has Ohio Avoided the Wake of MITE? An Analysis of the Constitutionality of the Ohio Control Share Acquisition Act*, 46 Ohio State L.J. 203 (1985).

B. Control Share Acquisition Statutes, Such As The ICSAA And MCSAA, Do Not Offend The Commerce Clause Because They Neither Directly Regulate Nor Impose Clearly Excessive Burdens On Interstate Commerce.

The Commerce Clause prohibits an individual state from directly regulating or imposing clearly excessive burdens on interstate commerce. A state statute must therefore be upheld if it only indirectly impacts interstate commerce and any such burden is reasonable in relation to the local benefits derived from the state legislation. *Edgar v. MITE Corp.*, 457 U.S. 624, 640 (1982); *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970); *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440, 443 (1960). The control share acquisition statutes are constitutional because their impact on interstate commerce is indirect, as well as insignificant, in comparison to the local benefits derived from the laws.

1. The Control Share Acquisition Legislation Does Not Impose A Direct Burden On Interstate Commerce.

By their very terms, control share acquisition laws, like the ICSAA and MCSAA, do not directly burden interstate commerce. The legislation only applies to control share acquisitions in a domestic corporation which has certain additional connections with the state of incorporation.[13] As a result, the

[13] The ICSAA applies to a control share acquisition in an Indiana company having its principal place of business, principal office or substantial assets in Indiana, and which has a certain level of its outstanding shares owned by Indiana residents, *e.g.*, 10 percent. Ind. Code Ann. § 23-1-42-4 (Burns Cum. Supp. 1986). The MCSAA applies to an offer to acquire shares in a Minnesota corporation which has its principal place of business, or assets greater than $1,000,000, located in Minnesota. Minn. Stat. § 302A.011, subd. 8 (Supp. 1985).

scope of these business corporation statutes is limited to companies created under the law of the regulating state and having a further nexus with that state. The control share acquisition legislation, which is part of the states' respective corporate laws, therefore does not directly impact on interstate commerce.

A contrary conclusion would effectively invalidate all state corporation laws because, as indicated above, the critical basis for such laws is that the regulating state is the state of incorporation. If this nexus, in and of itself, was insufficient to establish the indirect nature of the state regulation on interstate commerce, the longstanding authority of the states to adopt business corporation statutes would be emasculated.

Indeed, many business transactions routinely regulated by state corporate laws involve factual circumstances where the only nexus to the regulating state is that the subject company is incorporated in that state. For example, a merger proposed by a New York company with a Minnesota corporation is subject to a vote of shareholders pursuant to the Minnesota Business Corporation Act, even though *no shareholders* of the Minnesota company reside in Minnesota. *See* Minn. Stat. § 302A.613 (1984). Likewise, a voting trust between New York and Alaskan residents is unquestionably subject to Minnesota law if the stock involved is issued by a Minnesota company. *See* Minn. Stat. § 302A.453 (1984).

A multitude of similar examples can be cited where state business corporation laws properly regulate the activities of people and entities not residing in the regulating state, based upon the sole fact that the involved company is incorporated in the regulating state. Clearly, no other nexus with the regulating state is required—just the state of incorporation is sufficient to allow a state to legislate under its business corporation statutes.

The opinion in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982) does not provide otherwise. The *MITE* decision involved an Illinois securities tender offer registration law, not a business corporation statute. A plurality of the Court found the legislation to constitute a direct burden on interstate commerce because it regulated beyond the permissible scope of state securities laws. The Illinois law attempted to require the registration of a tender offer for securities even though no shareholder of the target company resided in Illinois. As such, the traditional and long-accepted nexus for regulation of securities matters, *i.e.*, shareholder residency, as established in the case of *Hall v. Geiger-Jones*, 242 U.S. 539 (1917),[14] was not present in the Illinois law. Accordingly, the plurality opinion noted that if other states imposed laws like the Illinois legislation, a tender offer could be subject to the securities statutes of many different states. 457 U.S. at 642.

Contrary to the Illinois securities statute involved in *MITE*, as discussed previously, control share acquisition statutes, like the ICSAA and MCSAA, are a part of the respective state's business corporation laws and therefore contain a proper jurisdictional nexus based on the target company's state of incorporation. Further, in stark contrast to the concern expressed in the *MITE* plurality decision on direct regulation, since companies have only one state of incorporation, there is no danger that a multiplicity of state corporate laws will apply to a particular control share acquisition.

Thus, just like other state corporation law provisions, control share acquisition legislation, such as the ICSAA and MCSAA, does not directly regulate or burden interstate commerce.

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[14] The *Hall v. Geiger-Jones* decision was actually quoted and relied upon by the *MITE* direct burden plurality. 457 U.S. at 641.

2. The Control Share Acquisition Provisions Do Not Impose Clearly Excessive Burdens On Interstate Commerce.

Any indirect impact of the control share acquisition statutes on interstate commerce does not impose clearly excessive burdens in relation to the local purposes served by the state legislation. The real, concrete and substantial benefits underlying the laws far exceed any actual or speculative burden imposed by the legislation on interstate commerce.

a. The local benefits underlying the control share acquisition laws are real, concrete and substantial.

The control share acquisition legislation furthers several important local benefits. First, and most significant, in accordance with the historical concept of shareholder democracy, the state laws protect shareholders of domestic corporations by affording them the right to control the destiny of their company. Second, the legislation mitigates the coercive nature of control share acquisitions. Third, the statutes inhibit the abusive use of takeover tactics, thereby furthering shareholder rights. Fourth, the state enactments enhance the regulating state's business climate which, in turn, encourages businesses to incorporate in that state and shareholders to invest in businesses incorporated in that state.

i. Pursuant to the historical concept of shareholder democracy, the state laws protect domestic company shareholders by affording them the right to control the destiny of their company.

A transaction which results in a change in control of a corporation may have a dramatic effect upon that corporation, an effect which can certainly be as substantial as a mer-

ger or other form of extraordinary corporate transaction. The control share acquisition laws merely extend to the shareholders of the regulating state's corporations the same right already enjoyed in the merger context, *i.e.*, to vote on transactions which may materially affect their company. This right of collective shareholder approval, which is grounded in the fundamental concept of shareholder democracy, furthers important local benefits by providing shareholders of domestic corporations the opportunity to control the destiny of their company.

Just like a merger, a change in control can unquestionably impact the future course and direction of a company. Indeed, if an acquiring person effects a control share acquisition, it will direct the operations of the company, even though it may have no expertise in the company's areas of operation. Furthermore, as in many takeover cases, the acquiring person could then merge with the target, drain the company of its cash, and perhaps sell off assets of the resulting company.

The target company shareholders could, of course, for a number of different reasons, have a substantial and legitimate interest in seeing that their company is not so changed. For example, regardless of the offering price, shareholders may believe that the target company's potential, if its operations continue unchanged, far exceeds that price. Therefore, shareholders may well prefer to allow the company to continue in its present method and manner of operation so that the full economic potential of the company can be realized.

Notwithstanding the foregoing, it is claimed that a state does not have a legitimate interest in extending benefits to shareholders of a domestic company if those shareholders do not reside in the regulating state. Language from *Edgar v. MITE Corp.*, 457 U.S. 624, 644 (1982), is relied upon in sup-

port of this contention. Again, the *MITE* decision is inapposite.

As thoroughly discussed above, *MITE* pertained to state tender offer *securities* legislation which conferred protection on investors outside the regulating state, thereby exceeding the legitimate scope of a state securities disclosure statute. In contrast, the legislation under review in this case relates to the states' longstanding authority to regulate *domestic corporations* and thereby properly provides protection to all domestic company shareholders, no matter where they may reside. Certainly, the very purpose of domestic corporation statutes is to protect all of the company's shareholders. *E.g.*, *Wooster Republican Printing Co. v. Channel 17, Inc.*, 533 F. Supp. 601, 617 (W.D. Mo. 1981), *aff'd*, 682 F.2d 165 (8th Cir. 1982) (state corporate law "designed primarily for the purpose of protecting the interests of shareholders of the corporation"). *See also Western Land Corp. v. Crawford-Merz Co.*, 62 F.R.D. 550, 555 (D. Minn. 1973). As far as domestic corporation laws are concerned, the shareholders' states of residency are immaterial.

A different result would seriously undermine the states' previous longstanding and unquestioned authority to regulate domestic corporations. The multitude of shareholder protection provisions contained in state corporation statutes do not distinguish between domestic company shareholders who reside in the regulating state and those who reside elsewhere. For example, all domestic company shareholders can vote on a merger proposal, irrespective of their state of residency. State corporate laws apply even where not a single shareholder of the domestic company resides in the regulating state. *See, e.g.*, Minn. Stat. § 302A.613, subd. 2 (1984) (provides that all shareholders can vote on a proposed merger, without any

stated residency requirement). Clearly, the states' regulation of domestic corporations legitimately and properly benefits all domestic company shareholders, no matter where they reside.

It is also asserted that a change in control does not impact the internal affairs of a company. The basis for this contention is found in language from the *MITE* opinion which states that "[t]ender offers contemplate transfers of stock by shareholders to a third party and *do not themselves* implicate the internal affairs of the target company." 457 U.S. at 645 (emphasis added).

Reliance on this statement from *MITE* is misplaced. The state tender offer securities statute involved in *MITE* dealt with the process by which tender offers are made. The tender offer process quite clearly does not implicate the internal affairs of a company. Equally apparent, however, is the fact that control share acquisition provisions, like the ICSAA and MCSAA, do not regulate the tender offer process. Rather, these laws apply to the actual purchase of shares *following* a tender offer which would result in the acquiring person obtaining control in a domestic company. While tender offers *in and of themselves* do not affect the internal affairs of the subject corporation, a change in control clearly does implicate the internal affairs of the target company, as a typical takeover case so clearly demonstrates.

Once an acquiring person obtains control of a target company it will direct the operations of the company, even though the acquiring person may have no experience or expertise in the target's areas of operation. Further, with its acquisition of control, the acquiring person will have virtually unfettered discretion in how it changes the scope and structure of the target's business. This power, obtained upon acquisition of

control, clearly impacts on the future course and direction, let alone the very existence of the company. A corporation's internal affairs are most certainly implicated upon the consummation of a control share acquisition.

Nevertheless, it has been suggested that the internal affairs of a corporation are implicated only once the acquiring person votes its control block of stock, not at the time it consummates the control share acquisition.[15] This distinction elevates form over substance. Once control is obtained, the outcome of a shareholder vote is a foregone conclusion. In effect, the acquiring person controls the outcome of any shareholder vote and imposes its will on any minority shareholders. In the control share acquisition context, the concept of shareholder democracy can only be effectuated *before* acquisition of the controlling interest.

Finally, the contention that shareholder approval of a control share acquisition is not analogous to a shareholder vote on a merger transaction is without substance. It is apparent that for all practical purposes the transactions have an identical impact on the corporation. Without question, both mergers and control share acquisitions can have a profound effect on the future course and direction of the company.

In fact, the analogy between merger approval and control share acquisition approval is again made perfectly clear by the facts of a typical takeover case. It is common for an acquiring person to merge with the target without any mean-

[15] Although the ICSAA does not actually require shareholder approval prior to the control share acquisition, the practical effect of the Indiana statute may be just that. *See Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 261 (7th Cir. 1986). The MCSAA, of course, expressly requires shareholder approval prior to the consummation of a control share acquisition. Minn. Stat. § 302A.671, subd. 4 (Supp. 1985).

ingful vote by the target's shareholders. The first part, or front-end, of an acquiring person's plan is to gain control of the target through its tender offer. Upon obtaining control, the acquiring person will effect the second part, or back-end, of its plan, by the merger.[16] The outcome of the shareholder vote on the merger is a foregone conclusion due to the acquiring person's prior acquisition of control. As a result, the shareholders of the target will not have an opportunity to cast a vote, or at least a meaningful vote, as to whether the target and the acquiring person should be merged. Control share acquisition provisions, like the ICSAA and MCSAA, essentially fill this gap in the law.

ii. The state laws mitigate the coercive nature of control share acquisitions.

A control share acquisition confronts each shareholder, usually on short notice, with a "take it or leave it" proposition. In such an environment, an individual shareholder's decision to sell his or her stock does not necessarily amount to a vote in favor of the terms of the control share acquisition, nor does it mean that the shareholder would not prefer to remain as a shareholder of the existing company. To the contrary, individual shareholders, not knowing the position of other shareholders with respect to the proposed control share acquisition, may well sell their stock even though they oppose a change in control, because they fear that the proposed acquisition will succeed to the detriment of their company. Lacking the opportunity to decide on a collective basis whether the proposed acquisition is desirable, individual shareholders may be coerced

[16] *See, e.g., Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 255 (7th Cir. 1986); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 956 (Del. 1985).

into selling or tendering their shares when they would prefer to retain them.

A phenomenon commonly referred to as a "squeeze"[17] contributes further to this coercive environment. If a shareholder fails to sell his stock prior to the actual consummation of a control share acquisition, he will then be subject to a back-end merger whereby the acquiring person dictates the cash-out price. This cash-out price may be well below what the shareholder would have obtained by selling or tendering his shares prior to the consummation of the control share acquisition. Again, although a shareholder may prefer to retain his stock in the company, without knowing the position of other shareholders regarding the proposed acquisition, an individual shareholder can be squeezed into selling his or her stock.

The control share acquisition laws provide important, concrete and substantial local benefits[18] by mitigating the coer-

[17] *See, e.g., Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 255 (7th Cir. 1986).

[18] The benefits underlying the state legislation are not undermined due to the fact that a self-tender, a tender offer by the issuing company, is not subject to the state law. Control share acquisition laws do not apply to self-tenders for the obvious reason that, as a matter of definition, a self-tender does not change the ownership interest of the acquiring person, the issuing company. Certainly, the issuing corporation does not have a control interest in itself, and thus a self-tender, with its necessary increase of treasury stock, does not change the issuer's "control" of itself.

Further, state corporate law has traditionally recognized the right of a domestic corporation to repurchase its own shares. *See, e.g.*, Minn. Stat. § 302A.553 (1984). The directors must, of course, in repurchasing the company's stock, comport themselves in accordance with the fiduciary obligations owed to the shareholders. *See, e.g.*, Minn. Stat. § 302A.251, subd. 1 (1984). In contrast, a tender offeror seeking control owes no fiduciary obligations to shareholders.

It is apparent that the exclusion of self-tenders from the scope of control share acquisition laws is rationally based.

cive environment incidental to control share acquisitions. These benefits are effectuated by allowing shareholders of domestic corporations to collectively approve or disapprove the proposed acquisition. This process, based on the historical concept of shareholder democracy, provides domestic company shareholders the right to act in an informed, reasoned and non-coercive environment in deciding the fate of their company.

iii. The state statutes further the interests of shareholders by inhibiting the abusive use of takeover tactics by both offerors and target companies.

Control share acquisition statutes will have a beneficial impact by inhibiting the abusive use of takeover tactics by both offering and target companies. For example, a "poison pill"[19] is adopted and implemented by target company management without a shareholder vote, but in the professed best interest of shareholders.[20] Such defensive tactics, especially when used abusively, are almost always the subject of litigation which is usually considered by the courts on an expedited basis.[21] This litigation, in turn, places a tremendous burden on the courts and incredible expenses on the litigants, which expenses adversely affect target company shareholders. As a result, the courts are forced into the middle of these complex takeover battles and, instead of the shareholders, are effectively decid-

[19] The term "poison pill," as defined by the court of appeals, "refers to a family of shareholder rights agreements which, upon some triggering event such as the acquisition by a tender offeror of a certain percentage of the target corporation's common stock, entitle the remaining shareholders to receive additional shares of common stock (or other securities) at bargain prices." 794 F.2d at 254-55.

[20] *See, e.g., id.* at 255-56.

[21] *See, e.g., id.* at 251.

ing the eventual outcome of the takeover contest. Even more important, defensive measures of target companies oftentimes preclude the company's shareholders from considering an offer, even though a majority of the shareholders would find the offer attractive.

Control share acquisition legislation will, to a significant extent, remove the takeover battles from the courtroom and place the matter squarely before the most interested and affected parties, the shareholders. Certainly, target company management cannot as easily claim that "poison pills," or other defensive measures, are in the best interest of shareholders when a mechanism is readily available to enable the company's shareholders to vote on a proposed control share acquisition and thereby directly resolve the question for themselves. The mere presence of control share acquisition laws can therefore discourage the abusive use of defensive tactics by management.

The state legislation can actually be used affirmatively by offerors to bring the question of a control share acquisition directly to the shareholders, thereby bypassing the implementation of potentially abusive takeover tactics by target company management. If an offeror so chooses, it can invoke the law simply by filing the necessary information statement and thus force a shareholder vote on the proposed acquisition. Should the offeror prevail in the shareholder vote, it would be difficult, if not impossible, for target company management to employ defensive tactics to defeat the offer, if shareholders have already voiced their approval of the transaction.

Control share acquisition laws will similarly inhibit "greenmail,"[22] a common abusive purpose of offering companies.

[22] "Greenmail" has been defined as "[t]aking a large position in a company's stock, threatening a takeover, and then selling the shares back to the company at above-market prices. In short, it's

Payment of greenmail can economically devastate a target company and its shareholders, as well as deprive the shareholders from considering an offer they might otherwise approve.[23] Again, target company management cannot as readily agree to pay greenmail in the purported best interest of the shareholders when a process is available for the shareholders themselves to decide the propriety of the takeover transaction. As a consequence, an offering company cannot as easily extract greenmail from a target company, and therefore, the incidence of greenmail will presumably decrease dramatically due to the existence of control share acquisition legislation.

It is apparent, then, that the control share acquisition statutes provide real and substantial benefits by inhibiting abusive takeover practices, thereby enhancing the rights of shareholders.

iv. The legislation enhances a state's business climate.

The control share acquisition laws enhance a state's business climate, and, as a result, encourage investment in the regulating state and its domestic corporations. It is not disputed that the corporate takeovers can in a very short period dramatically alter a target company's business operations, whether it be, for example, the extortion of greenmail,[24] or merely the draining of the target's assets. The subject state

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a form of legal corporate blackmail." Reiser, *Corporate Takeovers: A Glossary of Terms & Tactics*, 89 Case & Com. 35, 44 (1984) (footnote omitted).

[23] *See, e.g.*, Note, *Exclusionary Tender Offers: A Reasonably Formulated Takeover Defense or A Discriminatory Attempt To Retain Control?*, 20 Ga. L. Rev. 627, 652-56 (1986); Note, *Greenmail: Targeted Stock Repurchases and the Management—Entrenchment Hypothesis*, 98 Harv. L. Rev. 1045, 1064-65 (1985).

[24] *See supra* note 22.

statutes afford to shareholders of domestic corporations the right to vote on control share acquisitions and thereby have some say in the future course and direction of their company. This ensures an orderly transition of control and power in the company pursuant to an informed and reasoned process wherein the shareholders have the ultimate voice in determining whether a change of control is best for their company.

It is important to note that promotion of a state's business climate is not premised upon precluding corporate raiders from moving business operations outside the regulating state. Instead, as indicated above, control share acquisition legislation promotes a state's business environment by providing an opportunity to shareholders of that state's corporations at least to participate in deciding the fate of their company. Due to the lightning-quick manner in which even longstanding shareholders, including the "founding fathers," of a corporation can be affected by a control share acquisition, extension of the shareholder democracy principle to these transactions is certainly attractive to businesses and their investors.

b. The burden on interstate commerce is insignificant in relation to the local benefits derived from control share acquisition legislation.

The burden imposed on interstate commerce by control share acquisition statutes is a limited restriction on an acquiring person in purchasing a particular amount of stock in a domestic company. The laws apply only to control share acquisitions, and even then they do not preclude such purchases. Rather, the legislation requires shareholder approval of control share acquisitions. Significantly, the control share acquisition provisions do not restrict other persons from buying or selling shares in the corporation.

Certainly, the burden on interstate commerce is no different than the one imposed by operation of corporate merger statutes. For example, a cash-out merger is clearly and constitutionally subject to shareholder approval.[25] Identical to the control share acquisition statutes, if a cash-out merger is collectively disapproved by shareholders, an individual shareholder is unable to sell his or her stock to the merging company in accordance with the proposed merger. This would be the case even if the merging company were a foreign corporation and no shareholders of the domestic company resided in the regulating state. Thus, the impact on interstate commerce is the same under a proposed control share acquisition and a cash-out merger.

Just as significant is that any burden on interstate commerce occasioned by the legislation is no greater than that imposed by state laws which require regulatory approval of control share acquisitions. Such laws can completely foreclose a transaction in interstate commerce. Yet, these state laws have been declared constitutional even though they impact on the ability of persons residing outside the regulating state to purchase stock in interstate commerce. *See, e.g., Baltimore Gas & Elec. Co. v. Heintz,* 760 F.2d 1408, 1421, 1427 (4th Cir.), *cert. denied,* 106 S. Ct. 141 (1985).

Furthermore, in the event a control share acquisition does not obtain shareholder approval, it is speculative whether the loss of such a transaction is actually a burden on interstate commerce. The recent rash of corporate takeovers shows that the economy and society in general are not always well served by such transactions. For example, greenmail, which is often incidental to and a purpose of a threatened control share acquisition, detrimentally affects both a target company and

[25] *See, e.g.,* Minn. Stat. § 302A.613, subd. 2 (1984); *Ashley v. Ryan,* 153 U.S. 436, 446 (1894).

its shareholders and furthers no worthy interest.[26] Discouraging these types of transactions serves to benefit, not burden, interstate commerce.

Presumably, if an acquiring person makes a reasonable proposal to the target company's shareholders, the proposed acquisition will be approved. Only those transactions that detrimentally impact on the company and its shareholders will fail to receive shareholder approval.

In measuring the alleged burden on interstate commerce, it must be recognized that a shareholder, no matter where he or she resides, purchases stock in a company subject to the laws of the state of incorporation. *See Broderick v. Rosner,* 294 U.S. 629, 644 (1935); *First National Bank v. Gustin-Minerva C.M. Company,* 42 Minn. 327, 328, 44 N.W. 198, 198-99 (1890). The domestic corporation laws effectively form a contract or charter between the corporation, its shareholders and the regulating state. *E.g., Aiple v. Twin City Barge & Towing Co.,* 274 Minn. 38, 46, 143 N.W.2d 374, 379 (1966); *Seitz v. Michel,* 148 Minn. 80, 84, 181 N.W. 102, 104 (1921). *See generally* 7A Fletcher, *Cyclopedia of Corporations,* § 3657 (Supp. 1986). Accordingly, as a matter of law, a shareholder purchases stock knowing full well that the incorporating state's corporate laws may impose restrictions on the accumulation of such stock.

Upon balancing the burden imposed by and benefits derived from the control share acquisition statutes, it is apparent that the legislation is constitutional. Like almost any state law, such as a corporate merger statute, the legislation under review in this case imposes some burden on interstate commerce. However, this burden is indirect and insignificant in relation to the benefits derived from the law. As a consequence, the

[26] *See supra* note 23.

burden imposed on interstate commerce by the law is *not clearly excessive* in comparison to the local benefits underlying the legislation.

II. CONTROL SHARE ACQUISITION LEGISLATION, SUCH AS THE ICSAA AND MCSAA, DOES NOT VIOLATE THE SUPREMACY CLAUSE.

It is undisputed that Congress has never expressed any intent to preempt state corporation laws, in the Williams Act or elsewhere, nor has it indicated any intent to occupy the entire field of such regulation. *See, e.g., Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906, 913 (8th Cir. 1984); *Agency Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029, 1036-37 (1st Cir. 1982). Because it is not physically impossible to comply with both the Williams Act and a control share acquisition law, the issue before the Court is whether state law so conflicts with the federal law that the state statute *substantially* frustrates the objectives of federal legislation. If not, the state law must be upheld. *See, e.g., Edgar v. MITE Corp.*, 457 U.S. 624, 632 (1982); *Florida Lime and Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963).

An examination of the state and federal laws demonstrates that the control share acquisition statutes do not frustrate, even in an insubstantial way, the purposes underlying the Williams Act. Indeed, the express objective and the timetable of the ICSAA, and certainly statutes like the MCSAA, are consistent with federal law. Moreover, the applicability of control share acquisition statutes to non-tender offer control share acquisitions does not conflict with the Williams Act.

A. The Objective Of Control Share Acquisition Laws, Such As The ICSAA And MCSAA, Is Consistent With, And Therefore Does Not Substantially Frustrate, The Purposes Of The Williams Act.

It is unquestioned that the principal and overriding objective of Congress in adopting the Williams Act was the protection of investors. *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 22-24 (1977); *National City Lines, Inc. v. LLC Corp.*, 687 F.2d 1122, 1129 (8th Cir. 1982); *Missouri Portland Cement Co. v. H.K. Porter Company, Inc.*, 535 F.2d 388, 393 (8th Cir. 1976). Similarly, control share acquisition legislation has been enacted to protect shareholders.[27] To accomplish this purpose, the laws impose the requirement that the shareholders vote on and approve the proposed acquisition.[28] As discussed previously, this requirement enhances the individual and collective rights of shareholders by allowing them, in accordance with the fundamental principle of shareholder democracy, to control the destiny of their company, by mitigating the coercive nature of control share acquisitions and by inhibiting the abusive use of takeover tactics. See *supra* at 11-20.

Not only do these state laws further the investor protection objective of the Williams Act, but they also do not disrupt the balance created by the Williams Act between the acquiring person and target company management.[29] Indeed, in promot-

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[27] For example, the Minnesota Legislature specifically stated that the MCSAA was intended to "provide to shareholders both necessary information and the opportunity to thus cast fully informed votes on any takeover transactions." Act of April 25, 1984, ch. 488, § 1, subd. 2(2), 1984 Minn. Laws 471.

[28] Ind. Code Ann. §§ 23-1-42-6 and -7 (Burns Cum. Supp. 1986), and Minn. Stat. § 302A.671, subds. 2 and 4 (Supp. 1985), as amended.

[29] *See Schreiber v. Burlington Northern, Inc.*, 105 S. Ct. 2458, 2463 (1985).

ing shareholders' interests by requiring collective shareholder approval of a control share acquisition, the legislation operates in an evenhanded manner. Both the offeror and management are subject to the same federal proxy rules and the same time constraints in presenting their respective positions to the shareholders. Consequently, the statutes favor neither management nor the offeror in presenting the proposed control share acquisition to a vote of the shareholders.

B. The Timetables Set Forth In Control Share Acquisition Legislation Like The ICSAA, And Particularly The MCSAA, Do Not Substantially Frustrate The Purposes Of The Williams Act.

The ICSAA is tailored to avoid any conflict with the procedural requirements of the Williams Act in the event a tender offer is made. The disclosure and voting requirements of the ICSAA are structured so they will be completed no later than 50 days after the information statement relating to the proposed acquisition is delivered to the target corporation.[30] As a result, the requirements of the ICSAA will be satisfied prior to the time that shareholders can, pursuant to the Williams Act, withdraw any tendered shares.[31]

Control share acquisition statutes like the MCSAA present an even clearer case of no conflict between the state and federal laws. Under the MCSAA, the required shareholder vote must be completed within twenty (20) business days of the

[30] Ind. Code Ann. § 23-1-42-7 (Burns Cum. Supp. 1986).

[31] Effectively, shareholders may withdraw any tendered shares for up to 15 business days after the tender offer is commenced or after 60 calendar days following commencement. Thus, under the Williams Act, the shareholder is unable to withdraw any tendered shares between the 16th business day and the 60th calendar day after the offer. 15 U.S.C.A. § 78n(d)(5) (1981) and 17 C.F.R. § 240.14d-7(a)(1) (1986).

target company's receipt of the information statement. Act of March 24, 1986, ch. 431, § 2, 1986 Minn. Laws 703. Accordingly, the Minnesota law does not conflict with the twenty (20) business day minimum period for an offer to remain open under the Williams Act,[32] as all state mandated procedures will be completed within the twenty (20) business day period. *See Cardiff Acquisition, Inc. v. Hatch*, 751 F.2d 906 (8th Cir. 1984). Hence, there is absolutely no delay occasioned by the Minnesota law in the consummation of a tender offer under the Williams Act.

The argument that the shareholder vote *could* be extended beyond the state law time frame because of *possible* delay in counting votes, or because of *possible* vote challenges, does not present a proper reason for invalidating the state legislation. Such speculative and hypothetical contentions cannot be a basis for deciding constitutional challenges. *See, e.g., Bardini Petroleum Co. v. Superior Court*, 284 U.S. 8, 22 (1931) ("Constitutional questions are not to be dealt with abstractly."). Moreover, even assuming, *arguendo*, that the Court could speculate as to potential for delay in the vote process, there is no showing that this hypothetical delay would constitute an "unreasonable delay," as envisioned by a plurality of the Court in *Edgar v. MITE Corp.*, 457 U.S. 624, 639 (1982).

It is also suggested that a control share acquisition statute is unconstitutional because it could preclude altogether the consummation of a tender offer if the acquiring person does not prevail in the shareholder vote. However, the Williams Act establishes no substantive federal right to purchase shares pursuant to a tender offer. *See, e.g., Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977); *AMCA International Corp.*

[32] 17 C.F.R. 240.14e-1 (1986).

v. Krause, 482 F. Supp. 929, 937 (S.D. Ohio 1979). It merely regulates the process by which an offeror must make his offer to purchase shares. The control share acquisition legislation does not interfere with this process. Rather, it simply accords to shareholders, on a collective basis, the right to approve or disapprove a change in control of their corporation—a transaction that can fundamentally alter the make-up and future of their corporation. To deprive shareholders of such an important right would be contrary to the traditionally democratic nature of corporate governance. To deny the states the power to grant such a right would be a dramatic departure from the historical role that states have played in regulating the corporations which they create.

C. The Applicability Of Control Share Acquisition Statutes To Non-Tender Offer Control Share Acquisitions Does Not Conflict With The Williams Act.

The Williams Act does not regulate non-tender offer transactions, such as open market purchases, except to the extent it requires any person who has accumulated more than five percent of a company's stock to make a Schedule 13D filing with the Securities and Exchange Commission. Section 13(d) of the Securities Exchange Act of 1934.[33] As such, the requirements of control share acquisition statutes do not conflict with the Section 13(d) disclosure provisions of the Williams Act and, for the reasons discussed above, actually further the investor protection purposes of the federal law. *See supra* at 11-20.

Nonetheless, it is suggested that the Williams Act, in a non-tender offer transaction, *implicitly* authorizes an open market

[33] 15 U.S.C.A. § 78m(d)(1) (1981). *See also* 17 C.F.R. § 240.13d-1 (1986).

or other acquisition of stock without any delay occasioned by state regulation. This argument is without merit.

Not only is it presumed that Congress did not preempt state law,[34] but there is simply no compelling indication that Congress, by its silence, intended to tacitly supersede state corporate laws. To the contrary, the Williams Act, in the non-tender offer context, only provides a disclosure mechanism relating to the accumulation of stock in a particular company. The federal law is by no means so pervasive as to preclude the states from invoking their historical authority to regulate domestic corporations.[35] *See, e.g., Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218 (1947).

As discussed previously, *see supra* at 14, the Williams Act regulates a different subject matter than do control share acquisition statutes. The federal law pertains to disclosures in the securities context, whereas the state law governs control share acquisitions which could materially impact on a domestic company's internal affairs. The federal and state laws, consistent with their traditional authority to regulate in their respective areas, constitutionally co-exist.

[34] *See, e.g., Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n.*, 461 U.S. 190, 206 (1983); *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981).

[35] This conclusion finds compelling support in *Agency Rent-A-Car, Inc. v. Connolly*, 686 F.2d 1029, 1036-37 (1st Cir. 1982). In that case, the court convincingly rejected the argument that Congress intended to occupy the entire field of control share acquisitions in adopting the Williams Act. The court therefore upheld, against a preemption challenge, a state law which regulated all methods of acquiring stock in a target corporation, whether by open market purchase, by solicitation of particular shareholders, by tender offer, or otherwise. In so doing, the First Circuit Court of Appeals recognized that Congress has not evinced an intent in the Williams Act, implicitly or otherwise, to preempt state law. 686 F.2d at 1036-37.

CONCLUSION

Based on the foregoing, *Amicus Curiae* State of Minnesota hereby requests that the Court reverse the decision of the Seventh Circuit Court of Appeals.

Dated: December 4, 1986.

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APPENDIX

Minn. Stat. § 302A.671 (Supp. 1985), as amended by Act of March 24, 1986, ch. 431, §§ 2 and 21, 1986 Minn. Laws 703, 706 provides:

302A.671 CONTROL SHARE ACQUISITIONS.

Subdivision 1. Authorization in articles. (a) Unless otherwise expressly provided in the articles or in bylaws approved by the shareholders of an issuing public corporation, this section does not apply to a control share acquisition.*

(b) All shares acquired by an acquiring person in violation of subdivision 4 shall be denied voting rights for one year after acquisition, the shares shall be nontransferable on the books of the corporation for one year after acquisition and the corporation shall, during the one-year period, have the option to call the shares for redemption at the price at which the shares were acquired. Such a redemption shall occur on the date set in the call notice but not later than 60 days after the call notice is given.

Subd. 2. Information statement. An acquiring person shall deliver to the issuing public corporation at its principal executive office an information statement containing all of the following:

(a) the identity of the acquiring person;

* This provision, Minn. Stat. § 302A.671, subd. 1(a), becomes effective on August 1, 1987, in accordance with Act of June 24, 1985, 1st Spec. Sess. ch. 5, § 21, 1985 Minn. Laws 1640 and Act of March 24, 1986, ch. 431, § 21, 1986 Minn. Laws 706. Minn. Stat. § 302A.671, subd. 1(a) as currently in effect is codified at Minn. Stat. § 302A.-671, subd. 1(a) (1984) and provides:

Subd. 1. Authorization in articles. (a) Unless otherwise expressly provided in the articles of an issuing public corporation, this section applies to a control share acquisition.

(b) a reference that the statement is made under this section;

(c) the number of shares of the issuing public corporation beneficially owned by the acquiring person;

(d) a specification of which of the following ranges of voting power in the election of directors would result from consummation of the control share acquisition:

(1) at least 20 percent but less than 33-1/3 percent;

(2) at least 33-1/3 percent but less than or equal to 50 percent;

(3) over 50 percent; and

(e) the terms of the proposed control share acquisition, including, but not limited to, the source of funds or other consideration and the material terms of the financial arrangements for the control share acquisition, plans or proposals of the acquiring person to liquidate the issuing public corporation, to sell all or substantially all of its assets, or merge it or exchange its shares with any other person, to change the location of its principal executive office or of a material portion of its business activities, to change materially its management or policies of employment, to alter materially its relationship with suppliers or customers or the communities in which it operates, or make any other material change in its business, corporate structure, management or personnel, and such other objective facts as would be substantially likely to affect the decision of a shareholder with respect to voting on the proposed control share acquisition.

Subd. 3. MEETING OF SHAREHOLDERS. Within five days after receipt of an information statement pursuant to subdivision 2, a special meeting of the shareholders of the issuing public corporation shall be called pursuant to section 302A.433, subdivision 1, to vote on the proposed control share acquisition. The meeting shall be held no later than 20 business days after receipt of the information statement, unless the acquiring person agrees to a later date. The notice of the meeting shall at a minimum be accompanied by a copy of the information statement and a statement disclosing that the board of directors of the issuing public corporation recommends acceptance of, expresses no opinion and is remaining neutral toward, recommends rejection of, or is unable to take a position with respect to the proposed control share acquisition. The notice of meeting shall be given at least ten days prior to the meeting.

Subd. 4. Consummation of control share acquisition. The acquiring person may consummate the proposed control share acquisition if and only if both of the following occur:

(1) the proposed control share acquisition is approved by the affirmative vote of the holders of a majority of the voting power of all shares entitled to vote.

A class or series of shares of the corporation is entitled to vote as a class or series if any provision of the control share acquisition would, if contained in a proposed amendment to the articles, entitle the class or series to vote as a class or series; and

(2) the proposed control share acquisition is consummated within 180 days after shareholder approval.

Subd. 5. Rights of action. An acquiring person, an issuing public corporation, and shareholders of an issuing public corporation may sue at law or in equity to enforce the provisions of this section and section 302A.449, subdivision 7.

Subd. 6. Return of shares if acquisition not consummated. If the proposed control share acquisition is not consummated in accordance with this section, the acquiring person shall immediately return any and all shares held in anticipation of the

consummation to the shareholders from whom the person received the shares.

Minn. Stat. § 302A.449, subd. 7 (Supp. 1985), as amended by Act of March 24, 1986, ch. 431, § 1, 1986 Minn. Laws 703 provides:

Subd. 7. PROXY IN CONTROL SHARE ACQUISITION. Notwithstanding any contrary provision of this chapter, a proxy relating to a meeting of shareholders required under section 302A.671, subdivision 3, must be solicited separately from the offer to purchase or solicitation of an offer to sell shares of the issuing public corporation. Except for irrevocable proxies appointed in the regular course of business and not in connection with a control share acquisition, all proxies appointed for or in connection with the shareholder authorization of a control share acquisition pursuant to section 302A.671 shall be at all times terminable at will prior to the obtaining of the shareholder authorization, whether or not the proxy is coupled with an interest. Without affecting any vote previously taken, the proxy may be terminated in any manner permitted by subdivision 3, or by giving oral notice of the termination in the open meeting of shareholders held pursuant to section 302A.671, subdivision 3. The presence at a meeting of the person appointing a proxy does not revoke the appointment.

Minn. Stat. § 302A.011, subds. 37-41 (1984 & Supp. 1985) (Definitions), provides:

Subd. 37. Acquiring person. "Acquiring person" means a person that is proposing to make a control share acquisition. When two or more persons act as a partnership, limited partnership, syndicate, or other group for purposes of acquiring, owning or voting securities of an issuing public corporation, the syndicate or group is a "person."

"Acquiring person" does not include a licensed broker/dealer or licensed underwriter who (1) purchases shares of an issuing public corporation solely for purposes of resale to the public; and (2) is not acting in concert with an acquiring person.

Subd. 38. Control share acquisition. "Control share acquisition" means an acquisition of shares of an issuing public corporation resulting in beneficial ownership by an acquiring person of a new range of voting power specified in section 302A.671, subdivision 2, paragraph (d), but does not include any of the following:

(1) an acquisition before, or pursuant to an agreement entered into before, August 1, 1984;

(2) an acquisition by a donee pursuant to an inter vivos gift not made to avoid section 302A.671 or by a distributee as defined in section 524.1-201, clause (10);

(3) an acquisition pursuant to a security agreement not created to avoid section 302A.671;

(4) an acquisition under sections 302A.601 to 302A.661, if the issuing public corporation is a party to the transaction; or

(5) an acquisition from the issuing public corporation.

Subd. 39. Issuing public corporation. "Issuing public corporation" means a corporation with at least 50 shareholders and which has either its principal place of business located in this state or owns or controls assets located within this state that have a fair market value of at least $1,000,000.

Subd. 40. Publicly held corporation. "Publicly held corporation" means a corporation that has a class of equity securities registered pursuant to section 12 of the Securities Exchange Act of 1934, as amended through December 31, 1984.

Subd. 41. Beneficial ownership. Beneficial owner includes, but is not limited to, any person who directly or indirectly through any contract, arrangement, understanding, relationship, or otherwise has or shares the power to vote or direct the voting of a security and the power to dispose of, or direct the disposition of, the security. "Beneficial ownership" includes, but is not limited to, the right, exercisable within 60 days, to acquire securities through the exercise of options, warrants, or rights or the conversion of convertible securities, or otherwise. The securities subject to these options, warrants, rights, or conversion privileges held by a person shall be deemed to be outstanding for the purpose of computing the percentage of outstanding securities of the class owned by this person, but shall not be deemed to be outstanding for the purpose of computing the percentage of the class owned by any other person. A person is the beneficial owner of securities beneficially owned by any relative or spouse or relative of the spouse residing in the home of this person, any trust or estate in which this person owns ten percent or more of the total beneficial interest or serves as trustee or executor, any corporation or entity in which this person owns ten percent or more of the equity, and any affiliate or associate of this person.

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In the Supreme Court of the United States

OCTOBER TERM, 1986

CTS CORPORATION, APPELLANT

v.

DYNAMICS CORPORATION OF AMERICA, ET AL.

STATE OF INDIANA, APPELLANT

v.

DYNAMICS CORPORATION OF AMERICA, ET AL.

ON APPEALS FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION AND THE UNITED STATES AS AMICI CURIAE

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QUESTION PRESENTED

Whether the Control Share Acquisitions Chapter of the Indiana Business Corporation Law is unconstitutional under the Supremacy Clause or the Commerce Clause of the United States Constitution.

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In the Supreme Court of the United States

OCTOBER TERM, 1986

No. 86-71

CTS CORPORATION, APPELLANT

v.

DYNAMICS CORPORATION OF AMERICA, ET AL.

No. 86-97

STATE OF INDIANA, APPELLANT

v.

DYNAMICS CORPORATION OF AMERICA, ET AL.

ON APPEALS FROM THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION AND THE UNITED STATES AS AMICI CURIAE

INTEREST OF THE SECURITIES AND EXCHANGE COMMISSION AND THE UNITED STATES

These appeals present the question whether the Control Share Acquisitions Chapter of the Indiana Business Corporation Law is constitutional as applied to "control share acquisitions" occurring in interstate commerce. The Securities and Exchange Commission and the United States submit this brief primarily to address the constitutionality of the Indiana statute under the Commerce Clause.

The Commission is responsible for the administration and enforcement of the federal securities laws, including

the regulation of national securities exchanges and other securities markets and the regulation of tender offers in interstate commerce. See generally Securities Exchange Act of 1934, 15 U.S.C. (& Supp. III) 78a *et seq.* As the federal agency primarily responsible for regulating the national securities marketplace in the public interest and for the protection of investors, the Commission has a substantial interest in the question whether a state law regulating "control share acquisitions" unconstitutionally burdens the national securities marketplace, which is an important part of interstate commerce.

The United States has an interest in proper interpretation of the role of the Commerce Clause in our federal system. The United States has an interest in both the free flow of commerce among the states and proper consideration of the prerogatives of the states.

STATEMENT

1. Appellant CTS Corporation (CTS) is an Indiana corporation with its principal place of business and substantial assets in Indiana (CTS J.S. App. A5). The common stock of CTS is listed for trading on the New York Stock Exchange (*ibid.*).[1] This case arises out of efforts of Dynamics Corporation of America (Dynamics), a publicly held corporation organized under the laws of New York, with its principal place of business in Connecticut, to acquire additional shares of stock in CTS by means of a tender offer (*ibid.*).

As of March 10, 1986, Dynamics was the beneficial owner of approximately 9.6% of the common stock of CTS, which was then selling at approximately $36 per share (CTS J.S. App. A1, A6, A13). On that date, Dynamics initiated a cash tender offer for another 1 million shares of CTS stock at $43 per share (*id.* at A1, A5). The addition of 1 million shares to the stock it already owned would give Dynamics a total of approximately 27.5% of the common stock of CTS (*id.* at A1). As required by the Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified at 15 U.S.C. 78m(d)-(e) and 78n(d)-(f)), Dynamics and CTS made certain filings with the Commission in connection with this tender offer.

[1] The common stock of CTS is registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78*l*(b) (CTS J.S. App. A5).

Also on March 10, Dynamics announced its intention to elect a full slate of nominees to the CTS board of directors at the annual shareholders meeting scheduled for the following month (CTS J.S. App. A31-A32; CTS Br. 2; Dynamics Mot. to Aff. 2). On the same day, Dynamics filed suit in the United States District Court for the Northern District of Illinois challenging CTS's proxy solicitations for the upcoming meeting (CTS J.S. App. A2).[2] The issues raised in the initial complaint are not before this Court.

2. Several days before the commencement of Dynamics' tender offer, the Governor of Indiana had signed into law a revised Indiana Business Corporation Law (Ind. Code Ann. §§ 23-1-17-1 to 23-1-54-2 (Burns Supp. 1986)), which included the Control Share Acquisitions Chapter (*id.* §§ 23-1-42-1 to -11).[3] Starting August 1, 1987, the new Business Corporation Law will apply to all Indiana corporations (Ind. Code Ann. § 23-1-17-3(a)), but corporations will be allowed to amend their articles of incorporation or bylaws to opt out of the Control Share Chapter (*id.* § 23-1-42-5). Before August 1, 1987, the statute is not automatically applicable but allows corporations to opt into the new Business Corporation Law, including its Control Share Acquisitions Chapter, by res-

[2] In its complaint, Dynamics sought to enjoin CTS's proxy solicitations as violative of Section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78n(a), and the Commission's rules thereunder (CTS J.S. App. A29-A30).

[3] The new law was signed on March 4, 1986. Hereafter, all citations to the Business Corporation Law and its Control Share Acquisitions Chapter will be to the version appearing in the 1986 Cumulative Supplement to Burns Indiana Statutes Annotated, Code Edition. The Control Share Acquisitions Chapter is reprinted in CTS J.S. App. A167-A188.

olution of the board of directors and without any shareholder action (*id.* § 23-1-17-3(b)). On March 27, 1986, the CTS board of directors by resolution opted into the new statute as of April 1, 1986 (CTS J.S. App. A2, A33).

Pursuant to the new law, shares acquired in an "issuing public corporation"[4] in excess of certain prescribed levels of voting power, termed "control shares,"[5] are stripped of all voting rights unless the shareholders of the corporation, in the manner described below, vote to restore voting power to the control shares (Ind. Code Ann. §§ 23-1-42-5, -9). The shareholders decide whether to restore voting power to the control shares either at the next special or annual meeting (*id.* § 23-1-42-7(c)) or at a special meeting called at the request of the person who proposes to make or has made a control share acquisition. Management of the subject company must schedule a special shareholders meeting within 50 days after the acquiror (1) delivers an "acquiring person statement" setting forth specified information; (2) requests such a meeting; and (3) provides an undertaking to pay the

[4] An "issuing public corporation" is defined as an Indiana corporation that has (1) 100 or more shareholders; (2) its principal place of business, its principal office, or substantial assets in Indiana; and (3) more than 10% of its shareholders resident in Indiana, or more than 10% of its shares owned by Indiana residents, or more than 10,000 of its shareholders resident in Indiana. Ind. Code Ann. §§ 23-1-20-5, 23-1-42-4(a).

[5] A "control share acquisition" is an acquisition of shares that causes the acquiror to cross the 20%, 33⅓%, or 50% threshold of voting power in an issuing public corporation. Ind. Code Ann. §§ 23-1-42-1, -2(a). "Control shares" are those acquired in such a transaction and any other shares acquired within 90 days or pursuant to a plan to make a control share acquisition. *Id.* §§ 23-1-42-1, -2(b). Dynamics' proposed acquisition would have crossed the 20% threshold. Certain acquisitions, such as acquisitions pursuant to the laws of descent and distribution, are excepted from the definition of "control share acquisition." *Id.* § 23-1-42-2(d) and (e). Acquisitions pursuant to an agreement of merger or plan of share exchange to which the corporation is a party are also excepted from the definition. *Id.* § 23-1-42-2(d) (5).

expenses of the meeting. *Id.* §§ 23-1-42-6 and -7. If the acquiror does not submit an acquiring person statement, or if the control shares are not given voting rights by the shareholders, then after a specified period the acquiror's shares may be redeemed by the subject company, if its articles of incorporation or bylaws permit (*id.* § 23-1-42-10).

In order for the control shares to get back their voting rights, the acquiror must prevail on two votes.[6] Under Ind. Code Ann. § 23-1-42-9(b)(1), there is a vote in which all shareholders of record are entitled to vote.[7] Under Ind. Code Ann. § 23-1-42-9(b)(2), there is a vote in which "interested shares" are disqualified from voting.[8] The acquiror will prevail only if, in each vote, the grant

[6] This appears to be the reasonable construction of the statute. The State, however, argues (Indiana Br. 29 n.*) that the new law requires two votes *only* "if the proposed control share acquisition would, if fully carried out, result in any of the changes described in IC 23-1-38-4(a)," relating to changes in the capital structure of the company.

[7] Section 23-1-42-9(b)(1) provides:

> To be approved under this section, the resolution must be approved by: * * * Each voting group entitled to vote separately on the proposal by a majority of all the votes entitled to be cast by that voting group, with the holders of the outstanding shares of a class being entitled to vote as a separate voting group if the proposed control share acquisition would, if fully carried out, result in any of the changes described in IC 23-1-38-4(a) * * *.

[8] "Interested shares" are defined in Ind. Code Ann. § 23-1-42-3 as shares owned by the acquiror, any officer of the issuing public corporation, or any employee of the issuing public corporation who is also a director. Shares held by directors who are not employees are not "interested shares" and may be voted in both votes. The requirement of a double victory poses a special problem for the acquiror: if it seeks to offset management-controlled shares in the "all-share" vote by buying tendered shares, these shares (which presumably would have been likely to vote in favor of the acquiror) will not be counted in the "disinterested share" vote.

of voting rights to the control shares is approved by a majority of the votes entitled to be cast.[9]

3. After the CTS board elected to be governed by the Control Share Acquisitions Chapter, Dynamics did not comply with the provisions of the Chapter but instead immediately amended its complaint in this action. Dynamics sought injunctive relief and a declaration that the Control Share Acquisitions Chapter was preempted by the Williams Act and imposed an unconstitutional burden on interstate commerce in violation of the Commerce Clause. CTS J.S. App. A2, A33-A34.

The district court entered an order on April 9, 1986, invalidating the Chapter as violative of the Supremacy Clause (CTS J.S. App. A87). In a second opinion, issued April 16, 1986, the district court ruled for Dynamics and against CTS on the additional ground that the statute impermissibly burdens interstate commerce (*id.* at A124, A139).

In an expedited appeal, the court of appeals affirmed both rulings of the district court (CTS J.S. App. A2, A28).[10] The court noted the dual-vote feature of the Control Share Chapter, *i.e.*, that "[a] decision in favor of awarding voting rights requires a majority both of all shares and of all 'disinterested' shares" and that, "[w]ithout these two majorities, the acquirer's shares remain nonvoting shares" (*id.* at A20). The court found it "fairly transparent" that the Chapter was drafted "to skirt judicial holdings that forbid states to delay tender offers beyond the period required by the Williams Act"

[9] In corporations with more than one class of stock, the approval must be given by a majority of the votes entitled to be cast in each "voting group," as defined in Ind. Code Ann. § 23-1-20-28. In the present case, because CTS has only one class of voting stock, there would be only one "voting group" for purposes of each of the two required votes.

[10] After the ruling of the court of appeals, Dynamics acquired tendered shares, increasing its ownership position in CTS to more than 27%. *Dynamics Corp. of America* v. *CTS Corp.*, 635 F. Supp. 1174, 1178 (N.D. Ill. 1986).

(*ibid.*), because an acquiror who is not interested in acquiring nonvoting shares is in effect forced to await the shareholders meeting before accepting tendered shares. "So he must hold the tender offer open for 50 days, rather than the 28 days required (on average) by the SEC's regulations under the Williams Act. * * * And he can have no great confidence in being able to win the vote on voting rights, since he cannot vote his own shares." *Ibid.*

The court of appeals explored the legislative history of the Williams Act and the substantial body of precedent interpreting it to forbid state legislation that adds delay to tender offers or otherwise upsets the balance that Congress struck between target management and tender offeror (CTS J.S. App. A21-A23). Despite admitting "doubts" about that precedent (*id.* at A23, A24), the court felt bound to follow it in light of *MITE Corp.* v. *Dixon*, 633 F.2d 486, 490-499 (7th Cir. 1980), aff'd on other grounds *sub nom. Edgar* v. *MITE Corp.*, 457 U.S. 624 (1982).[11] The court found it a "straightforward" matter to apply that precedent to invalidate the Chapter, since both the delay imposed by the Control Share Chapter and its shareholder-vote provisions were inimical to tender offers (CTS J.S. App. A23).

In deciding the Commerce Clause issue, the court weighed the local benefits provided by the Control Share Chapter against the burden that it places on interstate commerce (CTS J.S. App. A24-A27). The court found a burden on interstate commerce because "we can assume that the vast majority of both [CTS's] shareholders and Dynamics' shareholders are nonresidents [of Indiana, and t]he statute gravely impairs Dynamics' ability to do busi-

[11] Justice White's opinion in *MITE* reached the Williams Act issue and agreed with the Seventh Circuit (457 U.S. at 630-640), but that portion of the opinion was joined by only three Justices. The other two Justices who addressed the issue disagreed (*id.* at 646-647 (opinion of Powell, J.); *id.* at 655 (opinion of Stevens, J.)). See note 12, *infra*.

ness with any of CTS's shareholders" (*id.* at A25); because "the Indiana statute is calculated to impede transactions between residents of other states" (*ibid.*); and because "the efficiency with which [corporate assets] are employed * * * depends on the market for corporate control—an interstate, indeed international, market that the State of Indiana is not authorized to opt out of, as in effect it has done in this statute" (*id.* at A26 (citing *Edgar* v. *MITE Corp.*, 457 U.S. at 463 (opinion of the Court))). The court found no sufficient countervailing local benefit because "Indiana has no interest in protecting residents of Connecticut from being stampeded to tender their shares to Dynamics at $43" (CTS J.S. App. A25 (citing *MITE*, 457 U.S. at 642-643 (opinion of the Court))) and because residents of Indiana receive "trivial or even negative benefits" from the Control Share Chapter (CTS J.S. App. A25). The court rejected a claim that the "internal affairs" doctrine could save the statute, since "in this case the effect on the interstate market in securities and corporate control is direct, intended, and substantial; it is not merely the incidental effect of a general regulation of internal corporate governance" (*id.* at A27). Thus, the court held that the Control Share Chapter is invalid under the Commerce Clause.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Commission and the United States believe that the judgment of the court of appeals should be affirmed. This brief argues for affirmance only on the ground that the Chapter violates the Commerce Clause for a more specific reason than the reasons offered by the court of appeals.

The United States believes that the Indiana Chapter is not preempted by the Williams Act. As stated by appellant CTS (Br. 16-17), there is no conflict between any provision of the Williams Act and any provision of the Indiana Chapter that makes it impossible to comply with

both statutes. As also stated by appellant CTS (Br. 21-22), there is no preemptive federal statutory policy that the Indiana Chapter violates: the Williams Act was designed to favor neither the takeover bidder nor target management, see *Piper* v. *Chris-Craft Industries*, 430 U.S. 1, 29 (1977), but it does not prohibit states from adopting laws that operate to favor one side or the other, unless those laws conflict with the Williams Act or the Commission's regulations under that Act. Cf. *ibid.*

The Indiana Chapter does offend the Commerce Clause. It applies to "public" corporations, a category defined so as to consist, in substantial part, of corporations whose shares have been offered and sold in interstate commerce. CTS is such a corporation: its common stock is listed on the New York Stock Exchange. The central feature of the Indiana Chapter is an express restraint on certain transfers of the voting rights of such shares: the approval of "disinterested" shareholders is required before a willing seller may sell his voting rights to a willing purchaser in a transaction that meets the definition of "control share acquisition." As a practical matter, in all cases in which the buyer's objective is in fact "control," the Indiana Chapter makes that approval a precondition to the sale of the shares themselves.

A chartering state does not violate the Commerce Clause when it exercises its broad power to define, modify from time to time, and enforce the rights represented by shares of stock of the corporations it charters. In particular, a state may, in the exercise of its chartering function, require or permit voting rights to be distributed in a virtually limitless variety of ways: for example, a chartering state may provide (should it for some reason wish to do so) for a class of corporations in which no person may own more than 20% of the voting shares. A state performing its chartering functions does not offend the Commerce Clause, notwithstanding the obvious effects of the state's actions on the

value and transferability of shares of the corporations it charters, because the chartering state is responsible for the very existence of the corporation and its shares, and it may define the latter as it wishes notwithstanding effects on their transferability.

Indiana has done something different. The Indiana Chapter does not define (or permit the corporate draftsman to define) voting rights in a manner (however common or uncommon) equally applicable to whoever holds or acquires shares. It is written as a restraint on the transferability of voting rights in certain transactions, and it could not be written in any other way without changing its meaning. Its effect is to tend to preserve whatever pattern of voting rights (and, consequently, share ownership) exists in a given corporation at a given time against transactions that would alter the pattern.

The Indiana Chapter provides that whatever voting rights the corporate charter grants to shares, and whatever the pattern of ownership of those shares may now be, no share transaction in which the buyer crosses one of the three specified thresholds of share ownership will be effective to transfer voting rights without the consent of disinterested shareholders. For example, Shareholder A, who today owns 20.1% of the common stock of an Indiana corporation whose shares are listed on the New York Stock Exchange, may vote all of the shares, and may freely buy more (up to 33⅓%, the next threshold); but no person B who today holds less than 20% of the shares can freely cross the 20% threshold and catch up with A, because the transfer of voting rights to B in a threshold-crossing transaction is prohibited unless approved in a shareholder vote that will not include B but will (unless A is an officer or a director-employee of the corporation) include A. It is impossible to state the rule that produces this result as a rule of general applicability to both A and B: the positions of A and B are separated by a burden, imposed by Indiana, on the transfer from third parties to B of the voting

rights (and the shares that embody them) necessary to put B in the same position as A. Indiana is regulating not voting rights but transactions in interstate commerce.

In *Edgar* v. *MITE Corp.*, 457 U.S. 624, 643-644 (1982), the Court invalidated an Illinois statute that regulated interstate tender offers on the ground that the statute imposed a burden on interstate commerce for which (even as applied to Illinois corporations) there was no valid offsetting "legitimate local interest." In *MITE*, the Court rejected the two principal arguments offered by appellants in defense of the Indiana Chapter: the right of a chartering state to prescribe rules governing the internal affairs of the corporations it charters, and the right of a chartering state to protect the shareholders of such corporations. The Court said that the "internal affairs doctrine" is a "conflict of laws principle" of "little use to the State in [the tender offer] context. Tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company." *Id.* at 645. The Court also rejected the protection-of-shareholders argument on the ground that "the State has no legitimate interest in protecting nonresident shareholders. Insofar as the Illinois law burdens out-of-state transactions, there is nothing to be weighed in the balance to sustain the law." *Id.* at 644.

The United States believes that the language with which the Court in *MITE* rejected these two arguments was too broad. Prescribing rules governing corporate "internal affairs" and protecting the rights of shareholders are both valid and important activities of a chartering state. A corporation's chartering state is responsible for, inter alia, defining and enforcing the rights of all shareholders, both resident and nonresident, against the corporation, its directors and officers, and each other. Carrying out these responsibilities is an entirely legiti-

mate state function even though the state is necessarily projecting its law into interstate commerce whenever shares of a corporation it chartered are sold in the national marketplace.

Once it has defined the bundles of rights represented by shares and allowed the shares to enter interstate commerce, however, the chartering state does not have plenary power to define the circumstances under which the shares may be transferred. Such subsequent transfers, as this Court said in *MITE,* 457 U.S. at 645, "do not themselves implicate the internal affairs" of the corporation, and they therefore do not implicate the shareholder rights that the state is responsible for protecting.

Appellants seek to defend the Indiana Chapter on the ground that it merely deprives certain shares of voting rights under certain conditions and does not prohibit the transfer of anything. But as stated above the Indiana Chapter cannot be understood as a regulation of voting rights; it can only be coherently explained as a restraint on their transferability (and therefore on the transferability of the shares that embody them) in specified transactions. As the district court said, the Indiana Chapter "deprives the [control share] transaction of all value and therefore blocks the transaction in practical terms as much as would a direct prohibition on control acquisitions." CTS J.S. App. A79.

Appellants seek to distinguish *MITE* on the ground that the Illinois statute conferred power to block transactions on a state regulator, whereas the Indiana Chapter can be characterized as conferring a right on "disinterested" shareholders to participate in determining whether there will be an increase in the concentration of share ownership. We agree that this argument is not without substantial force. We nevertheless urge the Court to reject it on the ground that a state may not confer on shareholders a right that, inherently, is not a power to govern the corporation but a right to restrain interstate commerce.

ARGUMENT

THE INDIANA CONTROL SHARE ACQUISITIONS CHAPTER IS INVALID UNDER THE COMMERCE CLAUSE

INTRODUCTION

State regulation of takeovers and tender offers began with a Virginia statute passed in 1968. See L. Loss, *Fundamentals of Securities Regulation* 601 (1983). The impetus for the Virginia legislation and legislation that followed in other states was generally said to be "[f]ears that established local concerns might be taken over by outside interests which in turn would close down plants and leave local residents jobless." E. Aranow & H. Einhorn, *Tender Offers for Corporate Control* 153 (1973); accord L. Loss, *supra*, at 601. By 1977, a substantial majority of the states had enacted tender-offer legislation. See E. Aranow, H. Einhorn & G. Berlstein, *Developments in Tender Offers for Corporate Control* 207 (1977); see also L. Loss, *supra*, at 601-602 & n.120; Note, *Securities Law and the Constitution*: *State Tender Offer Statutes Reconsidered*, 88 Yale L.J. 510, 510 (1979). After one of these "first-generation" state takeover statutes failed to pass constitutional muster in *Edgar* v. *MITE Corp.*, 457 U.S. 624 (1982),[12] courts applied the Court's reasoning to invalidate similar statutes. See

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[12] In *MITE,* this Court held the Illinois Business Take-over Act unconstitutional on Commerce Clause grounds. The Illinois Act required a tender offeror to notify the Secretary of State of Illinois 20 business days before commencement of a tender offer. The Secretary of State was empowered to convene a hearing, and the tender offer could not proceed until that hearing was completed. One function of the hearing was to permit the Secretary to review the substantive fairness of the tender offer; if an offer was found "unfair," it could be permanently blocked.

The Court's Commerce Clause opinion, written by Justice White, had two branches. One branch stands as the opinion of the Court, joined by five Justices (Chief Justice Burger and Justices White, Powell, Stevens, and O'Connor). It held that the Illinois Act was invalid under the Commerce Clause because it placed a substantial

cases cited in 1 M. Lipton & E. Steinberger, *Takeovers & Freezeouts* § 5.02[4] (1984); L. Loss, *Fundamentals of Securities Regulation* 603 (1983 & Supp. 1986); Block, Barton & Roth, *State Takeover Statutes: The "Second Generation"*, 13 Sec. Reg. L.J. 332, 337-339 (1986); Warren, *Developments in State Takeover Regulation:* MITE *and its Aftermath*, 40 Bus. Law. 671, 686-694 (1985).

Since *MITE* and the lower court decisions following it, several state legislatures have reconstructed their regulatory schemes in an attempt to regulate takeovers in ways that will survive constitutional scrutiny.[13] A common theme of these statutes is that, instead of purporting to regulate takeover bidders' activities as such, they invoke the state's authority to regulate corporate structure and shareholders' rights. See L. Loss, *supra*, at 100 & n.129c (Supp. 1986). Some commentators still seek

burden on interstate commerce that outweighed any local benefits. 457 U.S. at 643-646.

In the other Commerce Clause branch of the opinion, joined by only four Justices (Chief Justice Burger and Justices White, Stevens, and O'Connor), the plurality concluded that the statute regulated interstate transactions taking place wholly outside of Illinois. Thus, the statute constituted a "direct" restraint on interstate commerce and was void even without an inquiry into the state interests involved. 457 U.S. at 641-643.

Three Justices (Chief Justice Burger and Justices White and Blackmun) found that the Illinois Act was invalid under the Supremacy Clause. 457 U.S. at 630-640. Two Justices (Justices Powell and Stevens) declined to join that holding. Three Justices (Justices Brennan, Marshall, and Rehnquist) believed that the case was moot and did not discuss the merits. *Id.* at 655-667. Justice Powell agreed that the case was moot but nevertheless joined the part of Justice White's opinion that constituted the opinion of the Court. *Id.* at 646-647.

[13] For a detailed discussion of these "second-generation" statutes, see 1 M. Lipton & E. Steinberger, *supra*, §§ 5.02-5.07; L. Loss, *supra*, at 99-101 (Supp. 1986); Block, Barton & Roth, *supra*, 13 Sec. Reg. L.J. at 339-354; Warren, *supra*, 40 Bus. Law. at 694-700; Sargent, *Do the Second-Generation State Takeover Statutes Violate the Commerce Clause?*, 8 Corp. L. Rev. 3, 5-6, 8-12 (1985).

to defend these statutes on the ground that they serve a legitimate local interest in preventing emigration of corporations and their assets. See, *e.g.*, Warren, *supra*, 40 Bus. Law. at 673 n.15; Newlin & Gilmer, *The Pennsylvania Shareholder Protection Act: A New State Approach to Deflecting Corporate Takeover Bids*, 40 Bus. Law. 111, 111-112 (1984). Others, however, defend them on the ground that they are merely a legitimate extension of more traditional forms of state corporation law. See, *e.g.*, Buxbaum, *Federalism and Company Law*, 82 Mich. L. Rev. 1163, 1175 (1984). Most courts that have ruled on the constitutionality of second-generation statutes have found them constitutionally infirm.[14] This case presents this Court with its first opportunity to pass on the constitutionality of a second-generation statute designed to avoid some of the problems that the *MITE* Court found with the first-generation statutes.

A. The Indiana Chapter Can Only Be Understood As A Restraint On Transactions In Voting Rights And The Shares That Embody Them

The Indiana Control Share Acquisitions Chapter prevents a shareholder of an Indiana "issuing public corporation," who may be situated anywhere in the nation, from conveying his voting rights to a buyer, wherever situated, in a "control share acquisition," unless two shareholder votes approve the conveyance. The category "issuing public corporation" is defined so as to include virtually every Indiana corporation that has offered and sold shares in interstate commerce (including appellant CTS). Most "control share acquisitions" would take

[14] See *Fleet Aerospace Corp.* v. *Holderman*, 796 F.2d 135 (6th Cir. 1986), appeal pending *sub nom. Ohio* v. *Fleet Aerospace*, No. 86-344; *Gelco Corp.* v. *Coniston Partners*, Civ. No. 3-86-847 (D. Minn. Nov. 10, 1986); *Terry* v. *Yamashita*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 92,845 (D. Hawaii June 13, 1986); *APL Ltd. Partnership* v. *Van Dusen Air, Inc.*, 622 F. Supp. 1216 (D. Minn. 1985), vacated as moot, No. 85-5285 (8th Cir. Nov. 26, 1985); *Icahn* v. *Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985).

place in interstate commerce. The Indiana Chapter expressly restrains the transfer of voting rights in such transactions, and its obvious practical consequence is to restrain the transfer of the shares as well.

Appellants contend that the Indiana Chapter merely defines voting rights in certain shares in certain situations, as the chartering state has plenary authority to do, and does not restrain interstate commerce except in the same incidental manner as many other state statutes defining shareholder rights. Although chartering states have broad authority to define shareholder voting rights,[15] that is not what Indiana has done in this case. The Indiana Chapter expressly restrains the transfer of whatever voting rights *do* attach to shares of an Indiana "issuing public corporation," and it could not, without changing its meaning, be written in any other way.

The Indiana Chapter expressly restrains only the transfer of voting rights, but the obvious practical effect of the Control Share Chapter, in every case with which it is concerned,[16] is to delay the sale of the shares themselves for up to 50 days, and bar it altogether unless the "disinterested" shareholders approve it. It is entirely incorrect to say that the Control Share Chapter "has utterly no effect on any shareholder's ability to *sell* his shares" (CTS Br. 39). As the district court said, "[b]y limiting the rights that a tender offeror [or, of course, any other acquiror] can purchase in a control [share] acquisition, the Indiana Act deprives the transaction of all value and therefore blocks the transaction in practical terms as much as would a direct prohibition on control [share] acquisition[s]" (CTS J.S. App. A79).

The Commerce Clause, of its own force, prohibits state-imposed restraints on transactions in interstate commerce in the absence of a substantial state interest served by the statute. At least since this Court's decision in *Cooley* v. *Board of Wardens*, 53 U.S. (12 How.) 298 (1851), it has been clear that the Commerce Clause[17] not only authorizes "'Congress to enact laws for the protection and encouragement of commerce among the states, but by its own force create[s] an area of trade free from interference by the States.'" *Great Atlantic & Pacific Tea Co.* v. *Cottrell*, 424 U.S. 366, 370-371 (1976) (quoting *Freeman* v. *Hewit*, 329 U.S. 249, 252

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[15] A chartering state may define, create, and limit corporate voting rights in ways that affect the attractiveness of shares without triggering any question under the Commerce Clause. The Commerce Clause does not require a state to define in any particular way the bundle of rights that will be put into interstate commerce as corporate shares. To the contrary, a corporation is a mere "'creature[] of state law'" (*Burks* v. *Lasker*, 441 U.S. 471, 478 (1979) (citations omitted)), and a share of stock has no inherent rights except those that state law and the relevant corporate documents give it. The district court's statement (CTS J.S. App. A79) that "[v]oting rights * * * [must be] an integral part of the ownership interest purchased along with a stock certificate" was quite wrong to the extent it meant that a state may not, for example, authorize nonvoting or restricted-vote stock.

[16] There can, of course, be share purchases that meet the definition of "control share acquisition" where the buyer is not interested in voting rights and thus will not be deterred by the shareholder approval provisions of the Chapter. But see Ind. Code Ann. § 23-1-42-10. The Chapter, however, is by its very terms aimed at transactions whose objective is "control." The fact that it also has an incidental impact on some transactions where the buyer is not seeking control does not alter the analysis.

[17] Congress is empowered, under the Commerce Clause of the Constitution, "[t]o regulate Commerce with foreign Nations, and among the several States." Art. I, § 8, Cl. 3. As the Court explained in *Hughes* v. *Oklahoma*, 441 U.S. 322, 325-326 (1979),

> [t]he few simple words of the Commerce Clause * * * reflected a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation.

See *Northeast Bancorp, Inc.* v. *Board of Governors of the Federal Reserve System*, 472 U.S. 159, 174 (1985); *South-Central Timber Development, Inc.* v. *Wunnicke*, 467 U.S. 82, 92 (1984); *H.P. Hood & Sons* v. *Du Mond*, 336 U.S. 525, 533 (1949); see also Eule, *Laying the Dormant Commerce Clause to Rest*, 91 Yale L.J. 425, 434-435 (1982).

(1946)); accord *Maine* v. *Taylor*, No. 85-62 (June 23, 1986), slip op. 6. There is a strong constitutional bias against direct state regulation of interstate markets. Interstate markets are generally to be left unregulated except to the extent that Congress chooses to regulate them. See *Hughes* v. *Alexandria Scrap Corp.*, 426 U.S. 794, 806 (1976) (dormant Commerce Clause protects "natural functioning of the interstate market" against state "prohibition or * * * burdensome regulation").[18]

The Indiana Chapter is not saved by the fact that it expressly restrains only the transfer of voting rights and not the transfer of shares. Direct restraints obviously must be judged by the items they reach, not merely the items they name: a direct restraint on transfers of steering wheels directly restrains transfers of automobiles as well. Cf. *Brown-Forman Distillers Corp.* v. *New York State Liquor Authority*, No. 84-2030 (June 3, 1986), slip op. 9 ("[t]hat the ABC Law is addressed only to sales of liquor in New York is irrelevant if the 'practical effect' of the law is to control liquor prices in

[18] The force of these Commerce Clause principles is not, as CTS asserts (CTS Br. 35), limited to situations in which a state has discriminated against interstate commerce or has imposed burdens on interstate commerce that may be duplicative of or inconsistent with burdens placed by other states. The argument that the Commerce Clause reaches only discriminatory state action was rejected in *Freeman* v. *Hewit*, 329 U.S. at 252, 254, and the argument that state action must pose a risk of multiple and inconsistent burdens was rejected in *id.* at 256-257. In that same case, the Court made clear that the Commerce Clause applies to the sale of shares of stock, even though shares of stock are only intangible property (*id.* at 258-259). On the other hand, as we suggest below, regulation by the state of incorporation of the sale of shares of stock (which was not at issue in *Freeman* v. *Hewit*) cannot be subjected to the same Commerce Clause analysis as state regulation of sales of tangible goods. As this Court has strongly indicated in a related context, the state as creator of the corporation has powers over the movement of its stock that it would not have over the movement of tangible goods. See *State Tax Commission* v. *Aldrich*, 316 U.S. 174, 180 (1942) (upholding against Due Process Clause challenge Utah tax on transfer at death of shares of stock in Utah corporation).

other States"); *Southern Pacific Co.* v. *Arizona*, 325 U.S. 761, 775 (1945).[19]

Indiana has broad authority to define the rights represented by the shares of its corporations and to define such rights in ways that may affect the value of the shares or the ease with which they may be transferred. But the Indiana Chapter does not provide that all shares, or some class of shares, of some or all Indiana corporations shall be without voting rights. Instead, Indiana has declared that whatever voting rights the corporate articles and bylaws confer may not be transferred in a "control share acquisition" except under specified conditions. The meaning of the Indiana Chapter cannot be explained without reference to the transactions that it restrains, and its effect is not to provide a general rule applicable to whatever persons hold or acquire shares but to protect whatever pattern of voting power (and, consequently, share ownership) exists in a given corporation at a given time against transactions that would alter the pattern. When a share of stock defined under Indiana law to represent certain rights has lawfully entered the national marketplace in securities, Indiana may not, under the Commerce Clause, directly restrain its further transfer in the absence of a substantial state interest.[20] The Indiana Chapter is such a direct restraint.

[19] The Court has repeatedly stated that "[t]he principal focus of inquiry [under the Commerce Clause] must be the practical operation of the [state] statute, since the validity of state laws must be judged chiefly in terms of their probable effects." *Lewis* v. *BT Investment Managers, Inc.*, 447 U.S. 27, 37 (1980); see *Hughes* v. *Oklahoma*, 441 U.S. 322, 336 (1979); *Dean Milk Co.* v. *City of Madison*, 340 U.S. 349, 354 (1951). This is not to say that every statute with an impact on a shareholder's ability to sell his shares is unconstitutional, or even requires any particular Commerce Clause scrutiny. But where a statute directly restrains the transfer of voting rights and the obvious practical effect of that bar is to restrain transfers of shares as well, the statute must be judged by its practical as well as its literal effects.

[20] This point does not depend on an assessment of the impact of the Control Share Chapter on economic efficiency. In *MITE* (457 U.S. at 643-644), the Court observed that economic efficiency is

B. The Broad Power Of A Chartering State To Govern The Internal Affairs And Protect The Shareholders Of Its Corporations Does Not Save The Indiana Chapter

While some of this Court's opinions have suggested that "direct" regulation of interstate commerce is unconstitutional without further inquiry (see, *e.g.*, *Brown-Forman Distillers Corp.* v. *New York State Liquor Authority*, No. 84-2030 (June 3, 1986), slip op. 5; *MITE*, 457 U.S. at 640 (plurality opinion); *Shafer* v. *Farmers Grain Co.*, 268 U.S. 189, 199 (1925)), the Court has in other cases suggested that the label "direct" does not always end the inquiry but instead exposes a statute to "more demanding scrutiny." *Maine v. Taylor*, No. 85-62 (June 23, 1986), slip op. 7. See *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Commission*, 461 U.S. 375, 390 (1983). At bottom, "the critical consideration is the overall effect of the statute on both local and interstate activity" (*Brown-Forman*, slip op. 5 (citing *Raymond Motor Transportation, Inc.* v. *Rice*, 434 U.S. 429, 440-441 (1978))). Just last Term, for example, in *Maine* v. *Taylor*, *supra*, the Court upheld a ban on fish importation that discriminates on its face against interstate commerce on the ground that importa-

poorly served by regulation that impedes takeovers. In the present case, the court of appeals (CTS J.S. App. A25) ruled that the Indiana statute is vulnerable to economic attack on the same grounds as the Illinois statute struck down in *MITE*. Cf. R. Winter, *Government and the Corporation* 42-44 (1978) (although economic efficiency is generally best served by allowing states broad latitude to enact corporation legislation, including even legislation that seems in isolation to run counter to the interests of efficiency, antitakeover legislation is an exception to that general rule). On the other hand, there are economic arguments that might be thought to support the Indiana legislation from an efficiency standpoint (see Indiana Br. 91-97, 100-101). The Constitution does not dictate that states, when acting within their proper spheres, act in accordance with any particular theory of economic efficiency, or that they pursue economic efficiency at all. The question in this case is whether the State of Indiana has acted within a proper sphere.

tion posed "significant threats to Maine's unique and fragile fisheries" that could not be otherwise countered. Slip op. 9-10 (footnote omitted).

An older example of a permissible state restraint on commerce is state blue sky laws, which typically prohibit the sale of securities into the regulating state or to its residents except on specified conditions. These statutes have been upheld as valid measures to protect a state's residents against fraud and other evils in the sale of securities, notwithstanding what the Court saw as an incidental effect on interstate commerce. *Hall* v. *Geiger-Jones Co.*, 242 U.S. 539, 554-556 (1917); *Merrick* v. *N.W. Halsey & Co.*, 242 U.S. 568, 590 (1917); *Caldwell* v. *Sioux Falls Stock Yards Co.*, 242 U.S. 559, 564-566 (1917). See *MITE*, 457 U.S. at 641 (plurality opinion); see also Loss, *The Conflict of Laws and the Blue Sky Laws*, 71 Harv. L. Rev. 209, 241-253 (1957).[21]

[21] While blue sky laws plainly affect interstate commerce, they differ from statutes like the Indiana Chapter in that they seek to protect state residents from a palpable harm to them from transactions with them that take place within the enacting state. One commentator points out that, "[u]nlike blue-sky laws, * * * which cover only intrastate transactions, takeover statutes reach tender offers, *wherever made*, if the target corporation, *not the transaction*, has certain contacts with the state." Kozyris, *Corporate Wars and Choice of Law*, 1985 Duke L.J. 1, 36 (footnote omitted); see Oldham, *Regulating the Regulators: Limitations upon a State's Ability to Regulate Corporations with Multistate Contacts*, 5 Del. J. Corp. L. 181, 242 (1980) (state tender-offer statutes, which "purport to govern offers made to shareholders regardless where domiciled," are "obviously more expansive than normal blue sky laws, which are limited to offers made to shareholders who reside in the state").

Contrary to CTS's contention (Br. 11-12, 34, 47), it is the blue sky cases rather than this case that resemble *Exxon Corp.* v. *Governor of Maryland*, 437 U.S. 117 (1978) (upholding Maryland's prohibition of ownership of retail service stations by gasoline producers and refiners). Like the law upheld in *Exxon* and unlike the Control Share Chapter in this case, blue sky laws regulate transactions that occur in the regulating state, and their interstate repercussions, although they indisputably exist, are indirect. This case, unlike *Exxon* and the blue sky cases, involves out-of-state transactions.

Appellants advance two reasons why the Control Share Chapter should be considered a legitimate form of state regulation.[22] First, the State asserts a general interest in regulating the "internal affairs" or "corporate governance" of Indiana corporations, and CTS appears to agree (Indiana Br. 81-86; see CTS Br. 39-40 & n.19). Second, both appellants argue that "[t]he Chapter serves the legitimate State interest of protecting non-dominant shareholders in Indiana corporations by allowing them to vote on a fundamental change in the corporation—its transformation from a company owned by scattered shareholders to one controlled by a single dominant shareholder" (CTS Br. 11; accord *id.* at 25, 37-38; Indiana Br. 88).

A chartering state does have a legitimate and substantial interest in governing the "internal affairs" of its corporations, including the rights of shareholders *vis-à-vis* the corporation itself, its directors and officers, and fellow shareholders. And having defined the rights of shareholders, a chartering state has an important and legitimate interest in protecting those rights with respect to all shareholders, resident and nonresident alike. A nonresident who buys shares in an Indiana corporation accepts that state's definition of his rights and buys that state's protection. See generally Buxbaum, *Federalism*

[22] The state alone suggests a third interest, a "strong interest in the welfare of employees of Indiana corporations with headquarters, factories or other operations in the State"; it argues that shareholders accordingly should be able to block a control share acquisition on the basis of "possible removal [of the corporation or its assets] from the State" (Indiana Br. 89-90). This asserted interest requires no extended discussion. If the dormant Commerce Clause means anything at all, it means that a state may not justify legislation on the ground that an impairment of commerce is necessary to prevent economic forces from moving resources out of that state and into another. See Levmore, *Interstate Exploitation and Judicial Intervention*, 69 Va. L. Rev. 563, 623-624 & n.240 (1983); Sargent, *Do the Second-Generation State Takeover Statutes Violate the Commerce Clause?*, 8 Corp. L. Rev. 3, 31 (1985); Note, *Securities Laws and the Constitution: State Tender Offer Statutes Reconsidered*, 88 Yale L.J. 510, 528 (1979).

and Company Law, 82 Mich. L. Rev. 1163, 1167 (1984); Levmore, *supra*, 69 Va. L. Rev. at 624.[23]

A chartering state's governance of the internal affairs of its corporations, including its definition of the rights of shareholders, obviously affects interstate commerce. Indeed, whenever the corporation then sells shares in interstate commerce, the chartering state may be said to be projecting its law beyond its borders.[24] Accordingly, much of corporation law properly comes within an

[23] In particular, in the absence of congressional action, it is a task for the state to define and enforce the fiduciary obligations of directors, officers, and controlling shareholders in connection with a tender offer. See *Schreiber* v. *Burlington Northern, Inc.*, 472 U.S. 1 (1985); cf. *Santa Fe Industries* v. *Green*, 430 U.S. 462 (1977); see also *Panter* v. *Marshall Field & Co.*, 646 F.2d 271 (7th Cir.), cert. denied, 454 U.S. 1092 (1981). See generally *Burks* v. *Lasker*, 441 U.S. 471 (1979). The Commerce Clause plainly does not *require* a state to enact legislation (or interpret its common law or legislation) to force corporate management to exercise its fiduciary duties in any particular way, a point the court of appeals made in a later chapter of this case. *Dynamics Corp. of America* v. *CTS Corp.*, 805 F.2d 705, 718 (7th Cir. 1986); see also CTS J.S. App. A10 (validity of "poison pills" is "a matter committed to the authority of the states"). The dormant Commerce Clause is a reservation to Congress of the exclusive right to legislate in certain ways affecting interstate commerce; it is not a command to states to legislate or adjudicate in any particular way.

[24] The traditional state-law provisions that appellants claim are threatened by the decision below all clearly relate to internal affairs and are clearly constitutional notwithstanding the fact that they are projected beyond the state's borders whenever the corporation sells shares in interstate commerce. For example, "the scheduling and voting methods for electing directors" and "restrictions on freeze-out or back-end mergers that may injure minority shareholders" (CTS Br. 49) relate, respectively, to corporate governance and to merger transactions to which the corporation itself is a party. These are legitimate matters of state regulation notwithstanding effects on the attractiveness of shares and consequent effects on transactions in those shares in interstate commerce. Similarly, a state statute that authorizes cumulative voting or staggered terms for directors of corporations incorporated in that state relates directly to corporate governance and raises no question under the Commerce Clause merely because it may make the shares more or less attractive.

exception to the principle that a state may not "project its legislation into" other states (*Baldwin* v. *G.A.F. Seelig, Inc.*, 294 U.S. 511, 521 (1935); *Brown-Forman*, slip op. 8-9), for the very placement of a security into interstate commerce is a projection of legislation into the home states of those who choose to buy the security.[25]

Moreover, the "internal affairs" of a corporation, including the rights of shareholders, of course comprise many matters that may bear on transactions in its shares. A few states have imposed on insiders a state-law fiduciary duty to the corporation or its shareholders not to sell or buy shares on the basis of undisclosed "inside information."[26] Controlling shareholders have a duty, at least in some states, not to sell control to a buyer who could be expected to loot the corporation.[27]

[25] Indeed, the application of a single state's law to the rights associated with a share of stock, wherever situated, contributes to the free flow of commerce in shares of stock. See *MITE*, 457 U.S. at 645 (opinion of the Court) (noting that "internal affairs doctrine," as a conflict-of-laws principle, fosters certainty in corporate relationships). This Court has observed that,

> as a general matter, the law of the state of incorporation normally determines issues relating to the *internal* affairs of a corporation. Application of that body of law achieves the need for certainty and predictability of result while generally protecting the justified expectations of parties with interests in the corporation.

First National City Bank v. *Banco Para El Comercio Exterior de Cuba*, 462 U.S. 611, 621 (1983); see also *Cort* v. *Ash*, 422 U.S. 66 (1975).

[26] See *Polin* v. *Conductron Corp.*, 552 F.2d 797, 810-811 (8th Cir.) (Delaware law), cert. denied, 434 U.S. 857 (1977); *Thomas* v. *Roblin Industries*, 520 F.2d 1393, 1397 (3d Cir. 1975) (Delaware law); *Davidge* v. *White*, 377 F. Supp. 1084, 1089 (S.D.N.Y. 1974) (Delaware law); *Diamond* v. *Oreamuno*, 24 N.Y.2d 494, 248 N.E.2d 910, 301 N.Y.S.2d 78 (1969); see also *Dirks* v. *SEC*, 463 U.S. 646, 672 (1983) (Blackmun, J., dissenting). But see *Freeman* v. *Decio*, 584 F.2d 186 (7th Cir. 1978) (Indiana law); *Schein* v. *Chasen*, 313 So. 2d 739, 746 (Fla. 1975). See generally Note, *Common Law Corporate Recovery for Trading on Non-Public Information*, 74 Colum. L. Rev. 269 (1974).

[27] See, *e.g.*, *Doleman* v. *Meiji Mutual Life Insurance Co.*, 727 F.2d 1480, 1483-1484 (9th Cir. 1984); *McDaniel* v. *Painter*, 418

And of course "internal affairs" also include the roles played by directors, shareholders, and others in approving or disapproving transactions between the corporation itself and other persons, including merger and acquisition transactions to which the corporation is a party.[28]

The question in this case is whether the Indiana Chapter *does* constitute regulation of "internal affairs." In *MITE*, the Court said that stock transactions between corporate shareholders and third parties do not "themselves" come under the heading "internal affairs." See

F.2d 545, 547-548 (10th Cir. 1969); *Insuranshares Corp.* v. *Northern Fiscal Corp.*, 35 F. Supp. 22 (E.D. Pa. 1940); *Ritchie* v. *McGrath*, 1 Kan. App. 2d 481, 486-488, 571 P.2d 17, 22 (1977); *Gerdes* v. *Reynolds*, 28 N.Y.S.2d 622, 652 (Sup. Ct. 1941); *Thompson* v. *Hambrick*, 508 S.W.2d 949, 953 (Tex. Civ. App. 1974), writ ref'd n.r.e; *Glass* v. *Glass*, 228 Va. 39, 47-48, 321 S.E.2d 69, 74 (1984). The chartering state can, of course, prohibit looting, and these cases impose liability on a shareholder who has abetted the looter. Cf. *Perlman* v. *Feldmann*, 219 F.2d 173, 179 (2d Cir. 1955) (Swan, J., dissenting) (knowledge or reasonable suspicion that buyer will loot the corporation "will terminate the dominant shareholder's privilege to sell and will create a duty not to transfer the power of management to such purchaser. The duty seems to me to resemble the obligation which everyone is under not to assist another to commit a tort rather than the obligation of a fiduciary.").

[28] Mergers and other "fundamental changes" that generally require shareholder approval are changes in the very structure of the corporation, and are accordingly an "internal" matter of legitimate interest to the state under the internal affairs doctrine. See *Fleet Aerospace Corp.* v. *Holderman*, 637 F. Supp. 742, 746 (S.D. Ohio), aff'd, 796 F.2d 135 (6th Cir. 1986), appeal pending *sub nom.* *Ohio* v. *Fleet Aerospace*, No. 86-344; *Gelco Corp.* v. *Coniston Partners*, Civ. No. 3-86-847 (D. Minn. Nov. 10, 1986). As one commentator has noted, "acquisitions of stock under a tender offer do not in themselves alter the corporate structure, procedures, and relationships, nor do they necessarily lead to a structural change; the acquirer may be content with control at the shareholder level. Furthermore, the tender offeror need not be a shareholder and the accepting offeree ceases to be one." Kozyris, *supra* note 21, 1985 Duke L.J. at 36-37 (footnote omitted). Any changes that an offeror making a control share acquisition *does* seek to make in the structure of the corporation are matters of internal affairs, and the state can require that shareholder approval be sought. See Ind. Code Ann. §§ 23-1-40-3, 23-1-41-2, 23-1-45-2.

MITE, 457 U.S. at 645 (opinion of the Court) ("Tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company.").[29] Illinois could not, the Court held, treat interstate commerce in shares of a public corporation as an internal matter and impose restraints on transactions between shareholders and third parties in the national securities marketplace. But, it is argued, the Illinois statute at issue in *MITE* was concededly a restraint on a class of interstate transactions —tender offers—whereas the Indiana Chapter, while it refers to a class of transactions (control share acquisitions) does not purport to bar transactions in shares but only to govern voting rights (normally an internal matter) in light of them. The Indiana Act cannot, however, be understood as an act merely defining voting rights. It is written as a restraint on the *transferability* of voting rights in specified transactions, and it could not be written in any other way without changing its meaning. Since the restraint on the transfer of voting rights is a restraint on the transfer of shares, the Indiana Chapter, like the Illinois Act, restrains "transfers of stock by stockholders to a third party."

Indiana argues that, by conferring the right to block the transfer on the shareholders themselves, rather than

[29] Accord *Great Western United Corp.* v. *Kidwell*, 577 F.2d 1256, 1280 n.53 (5th Cir. 1978), rev'd on venue grounds *sub nom. Leroy* v. *Great Western United Corp.*, 443 U.S. 173 (1979); see also *Restatement (Second) of Conflicts of Laws* § 302 comment e, at 310 (1971) (citing the transfer of stock as an example of matters that are not within the scope of "internal affairs regulation"); E. Aranow, H. Einhorn & G. Berlstein, *supra*, at 230; Wilner & Landy, *The Tender Trap: State Takeover Statutes and Their Constitutionality*, 45 Fordham L. Rev. 1, 17 (1976) (footnote omitted) ("[A] multistate tender offer has nothing to do with internal corporate procedures. Although transfer of control is the goal * * * it is accomplished in a tender offer without reference to the legal attributes of the domestic corporation. Hence, regardless of purpose, state regulation of an offer aimed at a domestic target is arguably unjustifiable, at least under the 'internal affairs' doctrine.").

a state official, it has created a scheme that is valid notwithstanding *MITE*. To put the argument in what we think is its strongest form, Indiana says that what it has done is to confer on all shareholders the right to participate in deciding whether the corporation in which they have invested goes from having (to use the current case as an example) a 9.6% shareholder to having a 27.5% shareholder. This argument is not without force, particularly since Indiana is quite correct that other shareholders may have a genuine interest in that transaction.[30]

[30] Shareholders may, of course, also benefit from transactions meeting the definition of "control share acquisition," and the procedures Indiana has required may deter bidders from entering into transactions that shareholders would favor. There has been a lively debate about whether measures that make takeover bids harder to accomplish harm shareholders in all cases. See, *e.g.*, Easterbrook & Fischel, *Auctions and Sunk Costs in Tender Offers*, 35 Stan. L. Rev. 1 (1982); Easterbrook & Fischel, *Corporate Control Transactions*, 91 Yale L.J. 698 (1982); Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 Harv. L. Rev. 1161 (1981); Manne, *Mergers and the Market for Corporate Control*, 73 J. Pol. Econ. 110 (1965); Ruback, *Assessing Competition in the Market for Corporate Acquisitions*, 11 J. Fin. Econ. 141 (1985) (all critical of defensive tactics); Bebchuk, *The Case for Facilitating Competing Tender Offers*, 95 Harv. L. Rev. 1028 (1982); Bebchuk, *The Case for Facilitating Competing Tender Offers: A Reply and Extension*, 35 Stan. L. Rev. 23 (1982) (some defensive tactics that lead to "auctions" are desirable, although author is generally in agreement with Easterbrook/Fischel objections to defensive tactics); Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics in Tender Offers*, 33 Stan. L. Rev. 819 (1981); Gilson, *Seeking Competitive Bids Versus Pure Passivity in Tender Offer Defense*, 35 Stan. L. Rev. 51 (1982) (same); Bradley & Rosenzweig, *Defensive Stock Repurchases*, 99 Harv. L. Rev. 1377 (1986) (some properly regulated defensive stock repurchases promote shareholder welfare); Lowenstein, *Pruning Deadwood in Hostile Takeovers: A Proposal for Legislation*, 83 Colum. L. Rev. 249 (1983) (arguing that both improper defensive tactics and coercive takeover tactics require legislative correction); Carney, *Shareholder Coordination Costs, Shark Repellents, and Takeout Mergers: The Case Against Fiduciary Duties*, 1983 Am. B. Found. Res. J. 341 (arguing that tender offers are often used by raiders

We think the Court should nevertheless reject this argument, on the ground that a state may not give shareholders of a public corporation the right to preserve the present pattern of share ownership against the operation of interstate commerce. An Indiana corporation whose shares are traded in the national securities marketplace remains a creature of Indiana law: many of its important attributes are determined by state law and are subject to modification by the state. But one of its important attributes, the identity of its shareowners and the size of their holdings, is (by virtue of the interstate sale of shares that Indiana allowed in the first place) a function of interstate commerce. An Indiana "public" corporation has, virtually by definition, raised capital by selling shares into the national securities marketplace. Raising capital in that manner is possible in part because that national marketplace enables shareowners to resell, and generally to trade in securities, in transactions determined by market forces, subject only to such regulation as Congress chooses to impose. Protecting that national market from intrusive state regulation is close to the heart of what the Commerce Clause is about.

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to expropriate the wealth of target shareholders); Lipton, *Takeover Bids in the Target's Boardroom*, 35 Bus. Law. 101 (1979); Lipton, *Takeover Bids in the Target's Boardroom: A Response to Professors Easterbrook and Fischel*, 55 N.Y.U. L. Rev. 1231 (1980); Lipton, *Takeover Bids in the Target's Boardroom: An Update After One Year*, 36 Bus. Law. 1017 (1981) (same). It has also been suggested that state antitakeover measures are more likely to have been enacted in order to protect incumbent management than to protect shareholders. See, *e.g.*, Winter, *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. Legal Studies 251, 268 (1977); Langevoort, *State Tender-Offer Legislation: Interests, Effects, and Political Competency*, 62 Cornell L. Rev. 213, 238-240 (1977); Loss, Foreword to Symposium, *Controlling Corporate Takeover Bids: State Regulation and the Ohio Approach*, 21 Case W. Res. L. Rev. 605, 609, 611 (1970). The court of appeals in this case engaged in second-guessing of the Indiana legislature on these issues. We think that was not the appropriate course, and that this Court's decision should not rest on a substitution of its judgment for that of the State of Indiana on where the best interests of shareholders lie.

CONCLUSION

The judgment of the court of appeals should be affirmed insofar as it rests on the ground that the Control Share Chapter is invalid under the Commerce Clause.

Respectfully submitted.

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NO. 86-71 & 86-97

IN THE
Supreme Court of the United States
OCTOBER TERM, 1986

CTS CORPORATION,
Appellant,
v.
DYNAMICS CORPORATION OF AMERICA,
Appellee.

STATE OF INDIANA,
Intervenor-Appellant,
v.
DYNAMICS CORPORATION OF AMERICA,
Appellee.

On Appeal From The United States Court Of Appeals For The Seventh Circuit

BRIEF AMICUS CURIAE OF UNITED SHAREHOLDERS ASSOCIATION IN SUPPORT OF APPELLEE

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MISCELLANEOUS

T. Boone Pickens United Shareholders Association (hereinafter "United Shareholders Association") respectfully submits this brief, with the consent of the parties, as Amicus Curiae in support of Appellee, Dynamics Corporation of America, to urge the Court to affirm the decision by the United States Court of Appeals for the Seventh Circuit which held that portions of the Indiana Business Corporation Law were unconstitutional under the Supremacy Clause and the Commerce Clause.

INTEREST OF AMICUS CURIAE

Amicus Curiae United Shareholders Association is a non-profit corporation organized and operated to:

(1) promote the welfare of the citizens of the United States of America by supporting the dissemination of ideas and actively encouraging legislative, regulatory, corporate and/or public reform in order to create lasting economic property and bolster the economic competitiveness of American business through the increased responsiveness and accountability of corporate management to shareholders;

(2) promote the public welfare by serving as an advocate before the general and shareholder public for the promotion of responsive, democratic corporate governance;

(3) heighten public awareness in the fields of responsible corporate governance and stockholders rights and the detrimental social and macroeconomic effects of the lack of responsive corporate governance; and

(4) further the ideals of responsible corporate governance and stockholders rights through the encouragement of the democratic operation of American business.

United Shareholders Association has an interest in this appeal because this Court's decision will have broad ramifications for all shareholders wishing to exercise their prerogative to participate in interstate transactions and to cast their individual votes in matters of corporate governance. The central issue presented to this Court is whether or not a state, cloaking itself in the veil of the regulation of corporate internal affairs, may delegate to incumbent corporate management the power to regulate significant interstate commercial transactions. The state cannot constitutionally exercise this power in its own right, yet it would authorize incumbent management to wield extensive powers directly affecting national markets. This deputization significantly interferes with interstate commercial transactions and subjects the individual shareholder to the tyranny of a management-controlled minority.

In contrast to those actions which are truly "internal" to the corporation, the individual shareholder here has no remedy for the actions management takes in compliance with the Indiana Control Share Acquisitions Chapter.[1] Thus, management and a few shareholders sympathetic to management are empowered to strip valuable property rights, the ability to tender shares with voting rights intact, from a target company's shareholders at the very moment that those rights attain their highest value for the shareholder.

1. Ind. Code Ann. §§ 23-1-42-1 to 11 (Burns Cum. Supp. 1986) (the "Control Share Chapter" or the "Chapter"). In matters of legitimate "internal affairs" a breach of fiduciary duty by management can be called into question by a derivative action brought by a shareholder on behalf of the corporation.

THE INDIANA CONTROL SHARE ACQUISITIONS CHAPTER

A summary of the relevant provisions of the Control Share Chapter is necessary in order for this Court to assess its deleterious effect upon significant interstate transactions and its obvious ability to frustrate the policies of the Williams Act.

Once a corporation has opted into the Chapter, the shares of that corporation acquired by a party in excess of certain ownership thresholds[2] are automatically stripped of their voting rights. Voting rights reattach *only* after completion of a process completely controlled by management.

If an acquiring person wishes to regain the voting rights ordinarily attendant to the excluded shares, he may request a shareholder meeting *and* undertake to pay the corporation's expenses at such special meeting. Within ten (10) days thereafter the incumbent directors must call a special meeting to be held *within fifty (50) days* after receipt of the request.[3] Management is not required to hold the special meeting before the scheduled expiration of any proposed tender offer and there is no provision allowing the offeror to accelerate the meeting. Similarly, no provision is made to bar the target corpora-

2. § 23-1-42-1. "*'Control shares' defined*": "'control shares' means shares that . . . when added to all other shares . . . owned by a person or in respect to which that person may exercise or direct the exercise of voting power, would entitle that person . . . to exercise or direct the exercise of the voting power of the . . . corporation . . . within any of the following ranges of voting power: (1) One-fifth (1/5) or more but less than one-third (1/3) of all voting power. (2) One-third (1/3) or more but less than a majority of all voting power. (3) A majority or more of all voting power."

3. § 23-1-42-7. "*Shareholder meeting to determine control share voting rights.*"

tion from taking defensive steps during the waiting period.[4] If no special meeting is requested, the voting rights to be accorded the shares acquired will be decided at the next special or annual meeting of shareholders.[5]

It is management's sole responsibility to prepare and take a position on a voting rights resolution, and to present the resolution to the shareholders.[6] The notice of the shareholder meeting is to include:

(i) a copy of the acquiring person's statement;

(ii) a statement by the Board of Directors of the corporation of its position or recommendation.[7]

No provision is made for any statement by, or solicitation on behalf of, the acquiring person.

Thus, fused upon the tender offer process is a proxy contest, with its potential for additional delay. Moreover, it is a proxy contest in which only the cossetted domestic corporation may solicit proxies. *Any proxies obtained by*

4. "According to the Securities & Exchange Commission, delay enables a target company to: (1) repurchase its own securities; (2) announce dividend increases or stock splits; (3) issue additional shares of stock; (4) acquire other companies to produce an anti-trust violation should the tender offer succeed; (5) arrange a defensive merger [target initiated transactions are specifically exempted from the Control Share Chapter. § 23-1-42-2(e)]; (6) enter into restrictive loan agreements; (7) institute litigation challenging the tender offer." *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d 558, 568 (6th Cir. 1982) (quoting *Edgar v. MITE Corp.*, 457 U.S. at 637 n.13, 102 S. Ct. at 2638, n.13). Additional defenses such as the increasingly popular "poison pills" are equally available to incumbent management.

5. § 23-1-42-7(c). *"Shareholder meeting to determine control share voting rights."*

6. § 23-1-42-7. *"Shareholder meeting to determine control share voting rights."* § 23-1-42-8. *"Notice of shareholder meeting."*

7. § 23-1-42-8. *"Notice of shareholder meeting."*

the acquiring person in support of the voting resolution fall within the definition of "interested share(s)," and are automatically stripped of voting rights.[8]

To pass, the voting resolution must be approved by:

(i) a majority of all shares; *and*

(ii) a majority of all *"disinterested"* shares.[9]

No deadline is imposed by the statute for the tallying of the shareholder vote, allowing management to further prolong the process beyond the fifty (50) day delay already provided management by the Control Share Chapter.

Voting rights reattach only to the extent granted by the resolution. If the resolution fails or if the acquiring person elects not to file an acquiring person's statement, the corporation may redeem the control shares at a "fair value thereof pursuant to the procedures adopted by the corporation."[10]

8. § 23-1-42-3. *"'Interested shares' defined."* ". . . '[I]nterested shares' means the shares of an issuing public corporation in respect of which [an acquiring person] *may exercise or direct the exercise* of the voting power of the corporation. . . ."

Read literally, the Chapter precludes not only uninvited tender offers but also proxy contests where the number of proxies obtained exceeds the statutory thresholds.

9. § 23-1-42-9. *"Resolution granting control share voting rights."* Unable to vote are those shares held by the acquiring person, officers of the corporation and any employees who are also directors. Those shares held by outside directors, who are clearly "interested" in any contest for control, are not excluded.

10. § 23-1-42-10-(a). *"Redemption of control shares."* Contrast to § 23-1-42-11(c), *"Rights of dissenting shareholders"* in which the fair value for the dissenting shareholder is defined as a value not less than the highest price paid per share by the acquiring person in a control share acquisition. No similar definition of fair value is included in Section 23-1-42-10, *"Redemption of control shares."* Instead, fair value is that value determined by the corporation.

SUMMARY OF ARGUMENT

Acting out of an excess of protectionistic zeal and in an effort to avoid this Court's decision in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), numerous state legislatures have rushed to enact second-generation takeover statutes,[11] of which the subject Control Share Chapter is but one example.[12] The impulse giving rise to such second-generation statutes, a putative interest in protecting local jobs and industry, constitutes exactly that type of economic isolationism and parochialism prohibited by the Commerce Clause of the United States Constitution. U.S. Const., art. I, § 8, cl. 3. Moreover, the second-generation statutes clash with and frustrate the Congressional policies embodied in the Williams Act, 15 U.S.C. §§ 78m (d)-(e), 78n(d)-(f), and thus violate the Supremacy Clause, U.S. Const., art. VI, cl. 2.

A statute that ostensibly regulates one type of transaction, but whose practical effect is to discourage or to interfere with another, must be tested for both Supremacy Clause and Commerce Clause purposes as though it regulated both transactions. That the inhibiting impact of the second-generation statutes arises out

11. *Control Share Acquisition Statutes*: Hawaii, Indiana, Maine, Minnesota, Missouri, Ohio, Pennsylvania and Utah.

Fair price legislation: Connecticut, Georgia, Illinois, Indiana, Kentucky, Louisiana, Maryland, Michigan, Mississippi, Missouri, New Jersey, New York, Pennsylvania, Virginia, Washington and Wisconsin.

12. The Control Share Chapter was passed in response to bids by nonresidents for two large Indiana corporations. 3 *Corporate Control Alert* 1, 10-11 (March 1986) (App. 141-142).

> When asked why Indiana had decided to adopt such a virulent statute, James Strain, an Indianapolis corporate lawyer from Barnes & Thornburg [counsel for Appellant CTS] said "We don't like having all our companies taken over by East Coast firms." On further reflection, Strain says Midwestern and West Coast acquirors are no better.

3 *Corporate Control Alert* 1, 10 (March 1986) (App. 141).

of practical impossibility and increased transaction costs rather than from an outright prohibition does not redress the imbalance, one at odds with the neutral position of the Williams Act. That the impact of the legislation flows from the regulation of voting rights after a control share acquisition, the "back end" of the transaction, rather than direct regulation of the offer, is constitutionally insignificant.

The Chapter was designed, drafted and intended to insulate Indiana corporations from the interstate market for corporate control.[13] The statute comes into play even if the tender offeror, the management of the target company and ninety percent of the company's shareholders are non-residents of Indiana.[14] The Commerce Clause ramifications are obvious. Out-of-state management of an Indiana corporation is permitted to strip the voting rights from shares tendered by out-of-state shareholders to an out-of-state offeror in response to a nationwide tender offer.

Unlike the Minnesota Act upheld in *Cardiff Acquisitions, Inc. v. Hatch*, 751 F.2d 906 (8th Cir. 1984), the Indiana Control Share Chapter is not closely tailored to advance the legitimate interests of Indiana. The dramatic sweep of the Chapter is exemplified by the fact that an individual residing in New York could not sell a twenty percent interest in an Indiana corporation to a California

13. See footnote 12, *supra*.

14. The percentage of non-resident shareholders could be much higher. By its terms, the Chapter applies if 10,000 Indiana residents hold shares in the company. CTS Corporation has 5,700,000 shares outstanding. If 10,000 Indiana residents each owned one share, the ownership of roughly .176% of the stock by Indiana residents would trigger the application of the Chapter. Indiana would then hold the interstate market for corporate control captive even though 99.824% of the shares were held by non-Indiana residents.

resident without being subject to the Chapter. That single sale, if the purchaser required that the shares be attended by voting rights, would require that the potential buyer file an acquiring person statement, request a special shareholder meeting, undertake to pay the expenses incurred in connection with such a meeting and then await the passage of fifty days (or more) for shareholder approval. The effect of the legislation upon interstate commercial activity is direct;[15] it is intended; it is substantial.

By its introduction of significant, indeed almost limitless, delay into the tender offer process, and its superimposition of a completely one-sided proxy contest upon the endeavor, the Chapter clashes directly with the Williams Act, decidedly tipping the scales in favor of the target corporation and its incumbent management and providing them with potent advantages with which to frustrate the pro-competitive effects of the tender offer effort.

The decision to take advantage of an offer, to receive a control premium for his or her shares, is no longer the independent economic decision of the individual shareholder. Instead, the investor is bound by the collective decision of the "disinterested" shareholders of the target company, presumably those who have not tendered and who are adverse to the offer. To this extent the Control Share Chapter offers illusory investor protection at the expense of investor autonomy.[16] If allowed to stand, this and similar legislation would lead inexorably to a Balkanization of the Nation's corporate economy.

15. Indiana concedes the direct impact of the statute upon tender offers by its extended discussion of alternative strategies foisted upon offerors. Brief of Intervenor-Appellant State of Indiana, pp. 63-68.

16. *Edgar v. MITE Corp.*, 457 U.S. at 639-640.

ARGUMENT

I. THE INDIANA CONTROL SHARE ACQUISITION CHAPTER VIOLATES THE COMMERCE CLAUSE.

The Control Share Chapter should be struck down as violative of the Commerce Clause. The Chapter's "avowed purpose" and "necessary tendency"[17] is to directly and substantially interfere with the interstate market for corporate control. The statute also violates the Commerce Clause by placing burdens upon interstate commerce which far outweigh the local benefits it purports to advance.

A. The Commerce Clause is Designed to Prevent the Balkanization of the Union and Prohibits Indiana from Regulating Interstate Commerce.

Through the years, this Court has been guided in its interpretation of the Commerce Clause by the basic principle that "our economic unit is the Nation." *H. P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 537 (1949). While some interference with the national economy may be tolerated when a state secures a cleaner, healthier, safer environment for its citizens,[18] this Court has often noted that simple economic protectionism is subject to a virtually *per se* rule of invalidity. *See, e.g., City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978).

Naturally, it is the rare state statute that boldly proclaims its purpose to be the advancement of parochial

17. *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 522 (1935).

18. Even in these areas of traditional local concern, however, the Court will accord less deference to the legislative judgment, "where the local regulation bears disproportionately on out-of-state residents and businesses." *Kassel v. Consolidated Freightways Corp. of Delaware*, 450 U.S. 662, 675-76 (1981).

local interests via direct discrimination against interstate commerce. However, a finding that state legislation constitutes "economic protectionism" may be made on the basis of either discriminatory purpose or discriminatory effect. *Bacchus Imports, Ltd. v. Dias,* 468 U.S. 263, ____, 104 S. Ct. 3049, 3055 (1984); *Minnesota v. Clover Leaf Creamery Co.,* 449 U.S. 456, 471 (1981). In analyzing state *economic* regulation under the Commerce Clause, the key consideration is the overall effect of the state law on both local and interstate activity. *Brown-Forman Distillers Corp. v. New York State Liquor Authority,* ____U.S.____, 106 S. Ct. 2080, 2084 (1986).

With the Control Share Chapter, Indiana has declared that *its* economic unit is Indiana. The state's avowed purpose is to "shield[] in-state industries from out-of-state competition," *Maine v. Taylor,* ____U.S.____, 106 S. Ct. 2440, 2453 (1986); the statute's natural tendency is to significantly depress the market for control of Indiana corporations.[19]

B. The Control Share Chapter Should be Struck Down as a Direct Violation of the Commerce Clause.

In *Brown-Forman, supra,* the Supreme Court reaffirmed that it has adopted a two-tiered approach to analyzing state economic regulation under the Commerce Clause.

> When a state statute directly regulates or discriminates against interstate commerce, *or when its effect is to favor in-state economic interests over out-of-state interests,* we have generally struck down the statute without further inquiry. . . . When, however, a statute has only indirect effects on interstate commerce and regulates evenhandedly, we have examined whether the State's interest is legitimate and whether the burden on interstate commerce clearly exceeds the local benefits. . . .

Brown-Forman, 106 S. Ct. at 2084 (emphasis supplied).

19. Needless to say, if this statute is valid, many or all of the other forty-nine (49) states will be pressured to enact similar legislation, in order to appease management of *their* domestic corporations. *See Edgar v. MITE Corp.,* 457 U.S. at 642.

While artfully drafted to avoid a simple comparison with the Illinois statute struck down in *Edgar v. MITE Corp.,* 457 U.S. 624 (1982), the Chapter is designed to directly regulate the interstate market for corporate control. This statute does not merely make it slightly more cumbersome for an uninvited suitor to take control of an Indiana corporation. Instead, the state has "overtly moved to slow or freeze the flow of commerce for protectionist reasons." *Philadelphia v. New Jersey,* 437 U.S. at 628. That Indiana deputizes the party most likely to obstruct interstate commerce to perform the interfering acts does not alter the analysis. To allow such a subterfuge to pass muster would be to glorify form over substance and "invite[] facile evasions of the [Commerce C]lause." *Dynamics Corp. of America v. CTS Corp.,* 794 F.2d 250, 264 (7th Cir. 1986).

The purpose of this statute is crystal clear. The origins of the statute[20] and the admissions made throughout the Brief of the State of Indiana show its true purpose: the shielding of Indiana corporations, Indiana jobs and Indiana industry from the effects of the interestate marketplace for corporate control.

Additionally, the Chapter effectively stymies tender offers for shares of Indiana corporations by forcing ac-

20. See footnote 12, *supra.*

quiring persons to overcome immense hurdles if they wish to exercise the most basic right adherent to their ownership interest in the corporation, the right to vote. The Chapter applies even though the acquiring person, the offerees and incumbent management are all non-residents of Indiana; it applies even though the corporation is headquartered outside of Indiana; it applies even though ninety percent (or more) of the shareholders reside outside Indiana; it applies if a hostile tender offer is commenced; and, it applies when a Florida owner of twenty percent of an Indiana corporation wishes to sell his shares to an Alaska purchaser. The practical effect of the Chapter is to regulate conduct far beyond the borders of the state. *Southern Pacific Co. v. Arizona,* 325 U.S. 761, 775 (1945); *Edgar v. MITE Corp.,* 457 U.S. at 643. This Chapter does not merely *rearrange* an interstate market among various entities engaged in interstate commerce. *See, e.g., Exxon Corp. v. Governor of Maryland,* 437 U.S. 117 (1978). It acts to *eliminate,* or at least greatly diminish, the interstate market for corporate control. The conclusion that the Indiana Control Share Acquisition Chapter is simple economic protectionism, designed to shield Indiana from the common market of the states, is inescapable.

C. The Burdens Imposed on Interstate Commerce by the Control Share Chapter Strongly Outweigh any Putative Local Benefits. The Chapter Advances no Benefits Which Are Not Better Served by Other Legislation.

This Court long ago made a pertinent observation:

> Nice distinctions have been made at times between direct and indirect burdens. They are irrelevant when the avowed purpose of the obstruction, as well as its necessary tendency, is to suppress or mitigate the consequences of competition between the states.

Baldwin v. G.A.F. Seelig, Inc., 294 U.S. 511, 522 (1935).

It is respectfully suggested that this Court disregard the "nice distinctions . . . between direct and indirect burdens" and declare this statute to be *per se* violative of the Commerce Clause. However, because this Court has observed that "no clear line separat[es] the category of state regulation that is virtually *per se* invalid under the Commerce Clause, and the category subject to the *Pike v. Bruce Church* balancing approach[,]" *Brown-Forman,* 106 S. Ct. at 2084, a discussion of the *Pike* test is also appropriate.

The *Pike v. Bruce Church* balancing test consists of two prongs:

> [1] Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. . . . If a legitimate local purpose is found, then the question becomes one of degree. [2] And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.

Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970). The allocation of the burden of proof when a statute is challenged was addressed in later cases.

> Once a state law is shown to discriminate against interstate commerce "either on its face or in practical effect," the burden falls on the State to demonstrate both that the statute "serves the legitimate local purpose," and that this purpose could not be served as well by available non-discriminatory means.

Maine v. Taylor, 106 S. Ct. at 2448.

1. The Burdens on Interstate Commerce Imposed by the Control Share Chapter Far Outweigh any Valid Interests Advanced by the Statute.

The direct burdens on interstate commerce imposed by the Chapter have been adequately described elsewhere.[21] The statute establishes nearly insuperable hurdles to prevent tender offerors, wherever resident, from transacting business with other shareholders.

To balance against this direct burden, Indiana suggests that the Chapter advances several state interests: (1) an interest in the welfare of employees of domestic corporations with headquarters, factories or other operations in the state; (2) an interest in "enacting the Indiana statute for the benefit of *all* shareholders of covered Indiana corporations"; and (3) an interest in protecting minority shareholders from the coercive effects of two-tiered tender offers.

What the state fails to recognize is that the protection of state jobs and industries, while a laudable goal, may not be advanced by the enactment of discriminatory legislation, the purpose and effect of which is to stifle interstate commerce. *Toomer v. Witsell,* 334 U.S. 385 (1948). "[T]he Court has viewed with particular sus-

21. *See ante*, pp. 3-5.

picion state statutes requiring business operations to be performed in the home state that could more efficiently be performed elsewhere. . . . [T]his particular burden on commerce has been declared to be virtually *per se* illegal." *Pike,* 397 U.S. at 145. While the state has every right to promote the economic welfare of its citizens, it cannot do so by erecting barriers to corporate control at the state borders. Our economic unit is the Nation; it must be Indiana's economic unit also.

The suggestion that Indiana has a legitimate interest in the welfare of *any* shareholder of an Indiana corporation, wherever resident, flies in the face of the majority opinion (Section V-B) in *Edgar v. MITE Corp.,* 457 U.S. at 644: "While protecting local investors is plainly a legitimate state objective, the State has no legitimate interest in protecting nonresident shareholders." In this regard, the emphasis placed by CTS and Indiana upon the "internal affairs doctrine" is misplaced. CTS and Indiana interpret this conflicts of law principle[22] as granting Indiana unfettered license to interfere with the national market for corporate control. But Indiana is granted no extraordinary interest in a corporation simply because that corporation has filed a few papers with the Indiana Secretary of State and pays a *de minimus* annual fee into the state coffers. Corporate voting rights do have their basis in state law, as Indiana notes, but these rights may not be regulated without regard to the effect on interstate commerce. "[T]he right to engage in interstate commerce is not the gift of a state. . . ." *Hughes v. Alexandria Scrap Corp.,* 426 U.S. 794, 808 (1976).

22. *Edgar v. MITE Corp.,* 457 U.S. at 645 (majority opinion).

In their haste to invoke the "internal affairs doctrine" as justification for the extensive regulation of interstate commerce, CTS and Indiana forget the teaching of this Court. "Tender offers contemplate transfers of stock by stockholders to a third party *and do not themselves implicate the internal affairs of the target company.*" *Edgar v. MITE Corp.*, 457 U.S. at 645 (majority opinion, emphasis added). Here Indiana regulates *shareholders,* not Indiana corporations. *Fleet Aerospace Corp. v. Holderman,* 637 F. Supp. 742, 763 (S.D. Ohio 1986), *aff'd* 796 F.2d 135 (6th Cir. 1986).

Perhaps most importantly, the Chapter, while denuding some shareholders of the right to vote their stock at the whim of management, does not advance the very interests it purports to protect. Nothing in the statute prevents *management* from selling Indiana assets, shutting down Indiana factories and eliminating Indiana jobs;[23] nothing in the Chapter protects minority shareholders from coercive two-tiered tender offers, so long as *management* is friendly to the offeror; finally, nothing in the Chapter prevents the great majority of shareholders from losing the potential benefits[24] of the interstate market for corporate control. *Dynamics v. CTS,* 794 F.2d at 264. The Chapter spells the demise of eminently fair "any and all" tender offers just as assuredly as it defeats two-tiered tender offers. The only distinction recognized by the statute is whether or not the bidder is friendly to management.

Thus, balanced against a directly intended, highly effective burden on interstate commerce is *one* putative bene-

23. *Fleet Aerospace,* 637 F. Supp. at 764.

24. *See* discussion of benefits of tender offers to shareholders in *Edgar v. MITE Corp.*, 457 U.S. at 643 (majority opinion).

fit—the protection of Indiana resident minority shareholders from coercive two-tiered tender offers. (While the *Pike* test envisions the Court weighing "putative local benefits," it need not weigh nonexistent or invalid concerns.) Where, as here, the burden on interstate commerce is direct, intended and substantial, the state has the burden of showing that its oppressive legislation would actually advance the state's only legitimate interest. Indiana has not done so;[25] instead, it has enacted a statute which interferes with the interstate market for corporate control, while leaving incumbent management free to alter the Indiana economic base as it pleases.

2. Any Legitimate Local Purpose Served by the Control Share Chapter could be Served as Well by Available Nondiscriminatory Means.

In its brief of December 4, 1986, Indiana omitted mention of the second prong of the *Pike v. Bruce Church* test:

> [T]he extent of the burden that will be tolerated will of course depend upon the nature of the local interest involved, *and on whether it could be promoted as well with a lesser impact on interestate activities.*

Pike, 397 U.S. at 142 (emphasis supplied). *See also, Maine v. Taylor,* 106 S. Ct. at 2448.

Here, the nature of the concern is the regulation of Indiana corporations. The state's interest in economic regulation is accorded a much lower status in Commerce Clause analysis than is its interest in safety regulations,

25. The state has indicated it has no evidence it wants to present. *Dynamics v. CTS,* 794 F.2d at 260.

health matters or the local environment. *H. P. Hood & Sons*, 336 U.S. at 533; *Sporhase v. Nebraska ex rel. Douglas*, 458 U.S. 941, 956 (1982). Significantly, Indiana has enacted two other statutes which purport to provide exactly that type of protection Indiana suggests is needed by shareholders of Indiana corporations. The Indiana Business Combination Statute[26] and the Dissenters' Rights Statute[27] both provide protection for minority shareholders caught in the "back end" of purportedly coercive two-tiered tender offers.[28] The Control Share Chapter, on the other hand, "protects" shareholders from the beneficial impact of fair tender offers, while providing no shareholder protection from the array of defensive maneuvers available to management.

II. THE CONTROL SHARE ACQUISITION STATUTE IS PREEMPTED BY THE WILLIAMS ACT.

Under the Supremacy Clause, the issue is whether Indiana's Control Share Chapter is preempted by the Williams Act. The Chapter is preempted because: (1) it conflicts directly with the requirements of the Williams Act;[29] and (2) it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in enacting the Williams Act.[30]

26. Chapter 23-1-43.

27. Chapter 23-1-44.

28. Amicus Curiae takes no position here on the wisdom or constitutionality of either statute.

29. *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963); *Franklin Nat'l Bank of Franklin Square v. People*, 347 U.S. 373 (1954).

30. *Hines v. Davidowitz*, 312 U.S. 52, 67-68 (1941).

The Control Share Chapter directly conflicts with the Williams Act by requiring the approval of a majority of "disinterested" shareholders before the objective of a tender offer can be fulfilled, i.e., the takeover of the company.[31] The mechanism by which such approval is obtained rests entirely in the hands of management.[32] The process is replete with an array of opportunities for delay, uncertainty and unfairness. The Chapter allows nationwide tender offers to be scuttled by a small minority of shareholders: (i) sufficient Indiana shareholders to invoke the Chapter and (ii) a majority of the "disinterested" shareholders, presumably those who oppose the offer. *See* footnote 14, *supra*.

The Chapter also conflicts with and frustrates the objectives of the Williams Act. The Williams Act is the product of intense investigation, discussion and compromise by Congress. Congress sought to promote fairness and protection of the investor-shareholder in the tender offer setting. It also considered the opportunities that should be available in our national free market system for incumbent management to retain its control of a company and for others to oust that management when they believe they can do a better job. This is the essence of the balancing of the Williams Act and the neutrality sought by Congress in the tender offer setting. The ". . . function of federal regulation is to get information to the investor by allowing both the offeror and the incumbent managers of a target company to present fully their arguments and then *to let the investor decide for*

31. Ind. Code Ann. § 23-1-42-9.

32. Ind. Code Ann. §§ 23-1-42-7, 8 and 10.

himself."[33] ". . . Congress intended for investors to be free to make their own decisions."[34] "Congressional policy is to permit the investor his own independent but informed decision whether to sell."[35]

A. The Control Share Chapter Conflicts Directly with the Requirements of the Williams Act.

One of the chief problems with the Chapter is the delay and uncertainty which it injects into the tender offer process. The Chapter allows management to delay a special shareholder meeting on the voting rights issue for at least fifty (50) days. No provision is made in the Chapter for the tallying of the vote on the resolution. During this time period, the potential acquiror cannot reasonably be expected to purchase any tendered shares—they have been stripped of their voting rights, rights restored only by a majority vote of the "disinterested" shareholders. Similarly, management cannot be expected to sit quietly during this time period. Undoubtedly, it will use the additional time to put various defensive measures in place, time which would be unavailable to it under the Williams Act.

In contrast to the almost unlimited delay provided for by the Control Share Chapter, the Williams Act permits the tender offeror to close an offer after twenty (20) business days. In drafting the Williams Act, Congress recognized that delay deters wealth-maximizing tender offers by giving entrenched management more time to

33. *Great Western United Corp. v. Kidwell*, 577 F.2d 1256, 1276 (5th Cir. 1978) *rev'd on venue grounds sub nom., Leroy v. Great Western United Corp.*, 443 U.S. 173 (1979) (emphasis added).

34. *Edgar v. MITE Corp.*, 457 U.S. 624, 639 (1982).

35. *Martin-Marietta Corp. v. Bendix Corp.*, 690 F.2d at 568.

implement defensive measures.[36] As noted previously, delay enables a target company to repurchase stock, enter into lock-up arrangements, announce dividend increases or stock splits, issue more stock, arrange defensive mergers, enter into restrictive loan agreements, institute litigation or take other action to increase the cost and uncertainty of the take-over attempt. *Martin-Marietta Corp., supra,* at 568.

The fact that the State of Indiana can conjure up a method by which tender offerors could hypothetically comply with both the Williams Act and the Indiana statute misses the mark entirely.[37] The Williams Act sets forth the obligations of a tender offeror seeking control of a company. Obviously, if an offeror wanted to, it could leave its offer open longer or it could heavily condition its acceptance of tendered shares, but the imposition of such delay, the creation of such uncertainty, upsets the balance and neutrality sought by the Williams Act, tipping the scales greatly in favor of management.

36. *Edgar v. MITE Corp.*, 457 U.S. at 636-38.

Congress continued to recognize the consequences of delay when it enacted the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 12 et seq.:

> [I]t is clear that the short waiting period [the 10-day proration period provided in § 14(d)(6) of the Securities Exchange Act of 1934 which applies only after a tender offer is commenced] was founded on congressional concern that a longer delay might unduly favor the target firm's incumbent management and permit them to frustrate many pro-competitive cash tenders. This ten-day waiting period thus underscores the basic purpose of the Williams Act—to maintain a neutral policy towards cash tender offers, by avoiding lengthy delays that might discourage their chances for success.

H.R. Rep. No. 94-1373, 94th Cong., 2d Sess. 12, *reprinted in* 1976 U.S. Code Cong. & A. News 2637, 2644.

37. Brief of Intervenor-Appellant State of Indiana, at 62-77.

The Chapter's approval process also superimposes a one-sided proxy contest on the tender offer. By stripping the voting rights of all shares or proxies tendered to the acquiror and by establishing a procedure whereby the so-called "disinterested" shareholders control the outcome of the resolution, the Chapter directly conflicts with the Congressional intent that the right to vote be a fundamental aspect of equity security ownership and with the atmosphere of "fair play" which Congress intended the proxy rules to foster.[38] As the court said in *Reserve Life Ins. Co. v. Provident Life Ins. Co.*, 499 F.2d 715, 725-26 (8th Cir. 1974), *cert. denied* 419 U.S. 1107 (1975):

> Under these [proxy] rules, an atmosphere of "fair play" must pervade the solicitation of proxies so that in struggles for corporate control, like the present one, competing interests are furnished equal opportunities to communicate with and thereby influence the shareholders in the exercise of their corporate suffrage rights.

Here management is given statutory license to exploit the proxy rules to delay offers beyond the fifty (50) days, thus injecting more uncertainty into the process. Moreover, under the Chapter, management has the exclusive right to present the voting rights issue to the shareholders and to take a position on the issue. No provision is made for the offeror to present its views nor can the acquiring person solicit any proxies in its own behalf. Any proxy granted the acquiring person would fall within the definition of "interested shares" and would automatically be

38. *J. I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964) ("fair corporate suffrage is an important right that should attach to every equity security bought on a public exchange").

stripped of voting rights.[39] Such a one-sided proxy solicitation directly conflicts with the Williams Act and the proxy rules promulgated thereunder.[40]

B. The Control Share Act Stands as an Obstacle to the Accomplishment of the Purposes and Objectives of the Williams Act.

As the State of New York so aptly pointed out in its brief,[41] the underlying objective of the Williams Act is the protection of investors. *See Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 29 (1977). Congress sought to protect investors by embracing a policy of strict neutrality between the bidder and management of the target company. In enacting the Williams Act:

> . . . Congress intended to strike a balance between the investor, management, and the takeover bidder. The bidder was to furnish the investor and the target company with adequate information but there was no "inten[tion] to do . . . more than give incumbent management an opportunity to express and explain its position." . . . Once that opportunity was extended, Congress anticipated that the investor, if he so chose, and the takeover bidder should be free to move forward within the time frame provided by Congress.

Edgar v. MITE Corp., 457 U.S. at 634. This policy of neutrality is "a major aspect of the effort to protect the

39. Ind. Code Ann. § 23-1-42-3.

40. See 15 U.S.C. § 78n.

41. Brief Amicus Curiae of the State of New York in Support of Appellants, at 9.

investor"; it complements the disclosure requirements and other investor protections of the Williams Act.[42]

The Control Share Chapter subverts this protection of investors by putting in place a management-controlled mechanism which makes virtually impossible any uninvited tender offer, regardless of the number of shareholders who favor it. It prevents the shareholder investor from tendering his shares for a premium to an acquiring entity if only a few shareholders in the corporation do not tender and those so-called "disinterested" shareholders vote against the tender offer. Thus, a minority of shareholders sympathetic to management can thwart a tender offer by voting not to restore the voting rights to the acquired shares, leaving the acquiring entity with the bleak prospect of owning a substantial block of stock stripped of the ability to take control of the corporation. The take-over is effectively scuttled, as is the ability of individual shareholders to sell their shares for a premium price. Such control over the outcome of a tender offer by management and those shareholders who may be sympathetic to management clearly upsets the balance of neutrality sought by Congress through the Williams Act.

The states' argument that such legislation encourages bidders to negotiate with incumbent management is a position unsupported by the Williams Act. There is no Congressional preference for negotiated take-overs at the expense of contested take-overs. State statutes that promote this objective, however laudable, must yield to Congress' determination. Contested take-overs should neither be encouraged nor discouraged.

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42. *Edgar v. MITE Corp.*, 457 U.S. at 633.

CONCLUSION

As Judge Posner aptly stated, "[t]he Indiana statute is a *lethal* dose [to constitutionally-protected tender offers]; the fact that the Illinois statute [struck down in *Edgar v. MITE Corp.*] may have been two or three lethal doses has no practical significance." *Dynamics Corp. of America v. CTS Corp.*, 794 F.2d 250, 262-63 (emphasis supplied). Judge Posner's assessment is accurate—after one lethal dose it is irrelevant how many more are administered. There is no difference between the Illinois statute struck down in *Edgar v. MITE Corp.*, in which a state agency was empowered to pass judgment on the fairness of a tender offer, and the Indiana Chapter in which the voting power of stock is stripped away until the "fairness" of the tender offer is passed upon by a jury of those who have already decided against tendering their shares.

The Chapter violates the Commerce Clause under both the direct regulation and the indirect burden analyses. It obtains no protection from the internal affairs doctrine. It is preempted by the Williams Act and thus violates the Supremacy Clause. This Court should affirm the judgment of the court below.

Respectfully submitted,

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Nos. 86-71 & 86-97

IN THE
Supreme Court of the United States
OCTOBER TERM, 1986

CTS CORPORATION,
Appellant,
—v.—
DYNAMICS CORPORATION OF AMERICA,
Appellee.

STATE OF INDIANA,
Intervenor-Appellant,
—v.—
DYNAMICS CORPORATION OF AMERICA,
Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

AMICUS CURIAE BRIEF OF THE SECURITIES INDUSTRY ASSOCIATION, INC. IN SUPPORT OF APPELLEE

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ON APPEAL FROM THE UNITED STATES COURT OF APPEALS
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AMICUS CURIAE BRIEF OF THE SECURITIES INDUSTRY ASSOCIATION, INC. IN SUPPORT OF APPELLEE

Pursuant to Rule 36.2 of this Court, and with the consent of the parties, The Securities Industry Association, Inc., submits this brief as *amicus curiae* in support of appellee Dynamics Corporation of America.

THE INTEREST OF THE SECURITIES INDUSTRY ASSOCIATION, INC.

The Securities Industry Association, Inc. ("SIA") is a trade association comprised of approximately 500 securities brokers and dealers transacting business both nationally and internationally. Its membership is responsible for over ninety percent of the securities brokerage business conducted in this country and includes members of every national securities exchange as well as securities firms that are not members of any exchanges.

SIA's members service securities investors of every size and type and perform a complete spectrum of professional securities activities, including retail and institutional brokerage, over-the-counter market making, underwriting and other investment banking activities, various exchange floor functions, and money management and investment advisory services. As a consequence, SIA is generally recognized as a spokesman for the securities industry in general and the broker-dealer community in particular.

The issues in this case involve the constitutionality of the so-called "second generation" of state takeover statutes, which are designed to regulate, and in most instances discourage, tender offers for corporate control other than those favored by incumbent management. These statutes purport to replace an earlier series of state tender offer statutes whose unconstitutionality was determined by this Court in *Edgar v. MITE*, 457 U.S. 624 (1982) ("*MITE*"). In fact, however, the efforts undertaken by the states since *MITE* to accommodate their takeover legislation to the concerns articulated by this Court in that case have been largely cosmetic. The primary purpose and effect of the state takeover statutes, to delay and deter unsolicited control acquisitions, has remained unaltered in the transition from the pre-*MITE* statutes to the more modern variety, of which the statute under review is a typical example.

As a recognized spokesman and representative of the securities industry on legislative and policy matters, SIA has regarded with growing concern the spectre of renewed efforts at local regulation of the national securities market by means of state takeover statutes. There are few economic phenomena less local and more national in character than tender offers for corporate control. Tender offers are offered on a non-discriminatory nationwide basis to all shareholders of a target corporation. Where large public corporations are involved, these shareholders will generally be found in nearly every state in the Union. Indeed, because the shares of such corporations are generally traded on a daily basis on one or another of the nationwide securities exchanges it is generally impossible to pinpoint, on a geographic basis, where all shareholders are located.

Shareholders who choose to accept an offer will generally send their acceptances and, eventually, their stock certificates, to the bidder's depository, whose offices will usually be located in one of the nation's major financial centers, outside the state of residence of most target shareholders and, more often than not, outside the state of domicile of either the bidder or the target corporation. Other shareholders, rather than awaiting completion of an offer which might be withdrawn or defeated, often choose to seek an immediate cash premium by selling their shares on the open market at a price that will have risen significantly in the wake of the tender offer announcement. Such trading, which guarantees many shareholders a profit even when an offer is withdrawn, usually takes place on the floor of a national exchange, which again is usually located in a state unrelated to the domicile of shareholder, target or bidder.

In the above ways and others, tender offers impact directly and substantially on the national securities market. The market factors and processes underlying these tender offers are consequently nationwide in character and—save for the impact of the local state statutes under review—are affected only slightly, if at all, by considerations specific to any single locality.

State attempts to regulate, and, in most cases, burden, nationwide tender offers occasion several negative results for

shareholders. In the first place, by discouraging and deterring tender offers, they deny to shareholders the premium values characteristic of such offers. Additionally, the threat, theoretical or actual, of a tender offer often forces an inefficient or insensitive management to respond more directly to shareholders' concerns with a consequential improvement in the market position of the corporation's stock. The removal of such threat is likely to have a depressing effect on the shares of such corporations and ultimately on the securities market as a whole. *MITE*, 457 U.S. at 643.

Furthermore, even where local statutes do not ultimately thwart a tender offer, they inevitably add a high level of confusion and uncertainty to the tender offer process. Under the federal scheme, set up by the Williams Act, the rules and processes for tender offers are clear, uniform, and straightforward. Brokers, dealers, investment advisors and the other members of the securities industry are generally conversant with their details. The superimposition upon this interstate framework of a variety of state regulatory schemes differing in their particulars cannot help but confuse shareholders and their investment advisors in reaching the economic decisions they must make with respect to their shares.

It is the position of SIA that tender offers, for all the controversy focused on them in recent years, are on the whole a beneficial influence on the national economy and on the national securities market. Even if additional regulation were thought to be necessary to deal with any abuses in the tender offer process, such regulation would be ultimately dysfunctional and detrimental to securities holders unless it were national in scope and operation. Through promulgation of the Williams Act, and through frequent consideration of additional legislation, Congress has shown itself equal to the task of providing the necessary regulation.

Conversely, local legislation, impacting upon and burdening nationwide tender offers, clearly interferes with the interstate commerce in corporate securities. Such legislation disturbs the existent federal regulatory framework established by Congress

with respect to tender offers and complicates any additional steps Congress may take with respect to regulating this interstate phenomenon. These considerations underlay this Court's decision in *MITE*, which effectively eliminated the first generation of state takeover legislation. It is respectfully submitted that these same considerations mandate a similar conclusion with respect to the statute under review, as well as with respect to all local statutes similarly devised to evade the effects of the *MITE* ruling.

SUMMARY OF ARGUMENT

During the 1960s, tender offers arose as an increasingly common method for the achievement of corporate control. Pursuant to this method of control acquisition, potential acquirors, by-passing the sometimes hostile managements of target corporations, placed their offers to purchase controlling interests in corporations directly before the target's shareholders. Although tender offers generally offered substantial premiums to shareholders, and, additionally, conferred economic benefits to the economy as a whole, *MITE*, 457 U.S. at 633, Congressional concern increased over the fact that, at the time, tender offers operated in a regulatory vacuum, outside the disclosure requirements of the federal securities laws, and with no specified time period in which they were required to remain open.

The legislative reaction was the Williams Act, whose underlying purpose was to regulate tender offers for the protection and benefit of shareholders faced with a request to tender their shares. While, in its formative stages, the proposed Williams Act legislation was infused with an avowedly pro-management viewpoint, Congress' increasing realization of the substantial economic benefits conferred by tender offers led it to adopt, instead, a regulatory scheme designed not to inhibit tender offers, but rather characterized by a strict neutrality between the interests of incumbent target management, on the one

hand, and those of the offeror on the other. *See MITE*, 457 U.S. at 633.[1] The Williams Act legislation, as ultimately adopted, provided that shareholders receive full and timely disclosure with respect to matters material to their investment decisions and that tender offers proceed within a time frame carefully calibrated to benefit neither bidder nor management.

In the years since the promulgation of the Williams Act, tender offers have become an increasingly significant phenomenon in our nation's economic life. While Congress has often been requested by groups responsive to existing corporate management to enact legislation more restrictive of hostile takeovers, it has consistently declined to upset the delicate neutral balance embodied in the Williams Act.

These efforts, however, have often found more sympathetic ears in the state legislatures, which bodies are, in any case, more easily subject to the influences and pressures of local corporations. Thus, although at the time of the promulgation of the Williams Act there existed virtually no state legislation purporting to regulate acquisitions of corporate control,[2] in the years following a large number of states adopted statutes specifically designed to regulate tender offers. In most instances these state takeover statutes imposed requirements more burdensome on offerors than those provided for in the federal statute. These sometimes took the form of additional disclosure obligations and requirements for prior administrative review and approval of tender offers. Almost universally, such statutes established time frames which virtually assured that tender offers could not be consummated during the time

1 The legislative history amply reveals that the promulgators of the Williams Act had no intention to inhibit tender offers and even believed that the act "might encourage them." Nor did Congress intend to deny to shareholders "the opportunities which result from the competitive bidding for a block of stock of a given company," 113 Cong. Rec. 24,665-6 (1967) (remarks of Sens. Williams and Javits).

2 In 1968, when the Williams Act was enacted, Virginia was the only state which had a takeover statute and its law had been recently passed and never enforced.

periods established under the Williams Act. While the constitutionality of such statutes was consistently challenged, these takeover statutes often provided target managements with effective tools to at least delay a hostile offer until a more secure defensive device could be implemented.

Finally, this Court, in *MITE*, addressed head-on the question of the constitutionality of the state takeover statutes. A clear majority of the Court held that the Illinois takeover statute violated the Commerce Clause of the Constitution by the impermissible restrictions it imposed upon interstate securities transactions. A plurality of the Court, additionally, held that the statute violated the Supremacy Clause of the Constitution by obstructing the regulatory scheme established by Congress in the Williams Act. With respect to each of these constitutional bases the operative impermissible characteristic of the statute was the same—that it operated to delay and impede nationwide tender offers for corporate control.

Following this Court's ruling in *MITE*, the state takeover statutes then extant were consistently struck down by the courts, or their enforcement abandoned by state regulatory commissions. Very recently, however, the investment community has witnessed the resurrection of the state takeover statutes in a different garb. Under the prodding of local corporate managements, states have increasingly adopted "second generation" takeover statutes variously labelled as "control share" statutes or "business combination" statutes. These statutes purport to regulate not the tender offer process itself, but rather the purchase of shares pursuant to such offers or the exercise of the essential rights of such shares following the purchase of corporate control.[3] While the statutes may vary in their particulars, their purpose and effect is identical—to delay,

3 "Control share" statutes generally provide that one seeking to purchase more than a specified percentage (often 20%) of a corporation's stock cannot complete such purchase absent the approval of a majority of the shareholders of the corporation. The potential acquiror is generally excluded from participating in such vote. The Indiana statute under review technically permits a sale transaction to occur

impede and ultimately thwart nationwide tender offers and corporate control acquisitions.

Any differences between these "second generation" statutes and the pre-*MITE* legislation they replaced are more apparent than real. As the Court of Appeals in the instant case noted, while such statutes are "[c]leverly drafted . . . to skirt judicial holdings that forbid states to delay tender offers beyond the period required by the Williams Act, *the cleverness is fairly transparent*." 794 F.2d at 261 (emphasis supplied). Where the purpose of a local statute is to delay and discourage hostile tender offers and where the direct effect of the statute is the same, the particular form and method utilized to achieve this result should not immunize the statute from constitutional attack. To hold otherwise would be to permit form to rule

prior to shareholder approval but blocks the transfer of any voting rights absent such approval.

"Business combination" statutes operate to block an acquiror's ability to undertake a wide series of corporate transactions for an extended period of time even if he has purchased most or all of the shares in a target corporation. Thus, Indiana's business combination statute, Ind. Code, § 23-1-43-1 *et seq.* (1986), which is not the subject of the instant appeal, limits the acquiror's ability to cause the corporation to engage in a wide number of corporate transactions, including mergers, liquidations and the sale, lease, exchange, mortgage, pledge, transfer or other disposition of assets or the issuance of dividends beyond stated percentages and stated amounts. These restrictions, however, apply only in the case of a hostile acquiror.

The purpose and effect of both types of statutes is to deter and discourage anyone from purchasing a control interest in a corporation. Thus, for example, while the State of New York in its *amicus* brief (at p. 9) seeks to characterize its own business combination statute as more neutral than the Indiana statute under review, the Governor's Program Memorandum, 1985 N.Y. Laws Chap. 915, accompanying the New York statute, candidly acknowledged that "the effect of the legislation" was "to encourage a potential acquiror to negotiate its proposed acquisition with the board of directors *and to discourage unilateral takeovers* that depend on the assets of the target." *Id.* at p. 8 (emphasis added).

We suggest that the Court, if it invalidates the Indiana control share statute, make it clear in its opinion that other statutes such as business combination statutes which similarly attempt to evade the *MITE* holding and impede takeovers will also not pass constitutional muster.

substance, and to open the door to facile evasions of the Court's constitutional ruling.[4]

It is respectfully submitted that *MITE* and its progeny are fully dispositive with respect to the Indiana statute and to the generality of "second generation" takeover statutes of which it is representative. The continued attempt to use these statutes to undermine federal policies and overstep constitutional boundaries can only be prevented by this Court's declaration, in unambiguous terms, of the plain unconstitutionality of any state legislation which obstructs the nationwide securities market by setting up delays and impediments to nationwide tender offers and other control acquisitions.

ARGUMENT

I. THE INDIANA STATUTE IS PREEMPTED BY THE WILLIAMS ACT

A. Under *Mite*, State Statutes Must Not Delay Or Impede Tender Offers

Under the preemption doctrine, which is founded upon the Supremacy Clause of the Constitution, a state law will be deemed unconstitutional where such law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941); *Jones v. Rath Packing Co.*, 430 U.S. 519, 526, 540-41 (1977). In *MITE*, a plurality of this Court held that a state statute whose terms operated to impede and delay nationwide tender offers was unconstitutional in that it constituted an

4 Not surprisingly, the courts which have considered the "second generation" state control acquisition statutes have, following *MITE*, ruled such statutes unconstitutional under either the Commerce or Supremacy Clauses of the Constitution or both. *See, e.g.*, in addition to the decision under review, *Fleet Aerospace Corp. v. Holderman*, 796 F.2d 135 (6th Cir. 1986); *Gelco Corp. v. Coniston Partners*, C.A. No. 3-86-847 (D. Minn. Nov. 10, 1986); *Icahn v. Blunt*, 612 F. Supp. 1400 (W.D. Mo. 1985); *APL Ltd. Partnership v. Van Dusen Air, Inc.* 622 F. Supp. 1216 (D. Minn. 1985); *Terry v. Yamashita*, 643 F. Supp. 161 (D. Hawaii 1986).

obstacle to the purposes and objectives of Congress in enacting the Williams Act which regulates the making and, in particular, the timing of such tender offers.

It is respectfully submitted that the plurality opinion in *MITE* was correct and that the same grounds and reasons which led the plurality to apply the preemption doctrine in *MITE* clearly mandate a finding of unconstitutionality with respect to the Indiana statute at issue here.

The plurality opinion in *MITE* held that the Illinois statute at issue in that case conflicted impermissibly with the Williams Act in that, in its pro-management leanings, it disturbed the balance of strict neutrality between management and offeror which Congress, in enacting the Williams Act, had determined to provide the best protection for shareholders in corporate control contests.

> There is no question that in imposing these requirements, Congress intended to protect investors. But it is also crystal clear that a major aspect of the effort to protect the investor was to avoid favoring either management or the takeover bidder. . . . As Senator Williams explained:
>
> > "We have taken extreme care to avoid tipping the scales either in favor of management or in favor of the person making the takeover bids."
>
> 113 Cong. Rec. 24,664 (1967). This policy of "evenhandedness" represented a conviction that neither side in the contest should be extended additional advantages vis-a-vis the investor, who, if furnished with adequate information, would be in a position to make his own informed choice. We, therefore, agree with the Court of Appeals that *Congress sought to protect the investor not only by furnishing him with the necessary information but also by withholding from management or the bidder any undue advantage that could frustrate the exercise of an informed choice.*

457 U.S. at 633-34 (emphasis supplied) (citations omitted).[5]

A particular element of this carefully balanced approach adopted by Congress with respect to tender offers involved granting to the target's shareholders sufficient time to receive and digest the informational materials required to be distributed under the Williams Act while, at the same time, not permitting tender offers to be so delayed as to impede their consummation or grant to target management an undue advantage in resisting takeover attempts.

> . . . Congress intended to strike a balance between the investor, management and the takeover bidder. The bidder was to furnish the investor and the target company with adequate information but there was no "inten[tion] to do . . . more than give incumbent management an opportunity to express and explain its position." Once that opportunity was extended, Congress anticipated that the investor, if he so chose, and the takeover bidder should be free to move forward *within the time frame provided by Congress.*

Id. at 634 (emphasis added) (citations omitted).

Noting that "[d]elay has been characterized as the most potent weapon in a tender offer fight" (*id.* at 637 n.12), the plurality of this Court concluded, on the basis of the legislative history of the Williams Act as well as subsequent Congressional expressions of policy, that timing was an integral element of the legislative scheme inherent in the Williams Act. Indeed the plurality in *MITE* concluded, correctly we submit, that the Illinois statute violated the Supremacy Clause precisely

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5 The clear intendment of Congress to adhere to a policy of strict neutrality in corporate control contests was recently reaffirmed by the unanimous opinion of this Court:

> The expressed legislative intent [of the Williams Act] was to preserve a neutral setting in which the contenders could fully present their arguments.

Schreiber v. Burlington Northern, Inc., 105 S. Ct. 2458, 2463 (1985).

by reason of the fact that the provisions of such statute contained the potential for delays greater than that provided in the time framework mandated under the Williams Act. *Id.* at 639.[6]

B. The Second Generation Statutes Violate The Williams Act's Policy Of Neutrality

In the instant case the shareholder vote provisions of the Indiana statute similarly offend against the time-frame mandated by the Williams Act by virtually assuring that any tender offer conducted pursuant to the Indiana statute will be subject to delays greater than those established by the Williams Act. The statute further provides that the ability to engender such delays shall lie exclusively in the hands of target management. In this manner the careful neutral balance which this Court has recognized to be the essential policy of the Williams Act is overthrown.

Appellants' attempts to reconcile the Indiana statute with the Williams Act are unavailing. Thus, they argue that the potential fifty-day delay imposed on bidders under the statute is no greater a burden upon tender offers than the delays imposed when bidders must leave their offers open due to the necessity of obtaining prior state or federal regulatory approvals, such as those required, for example, under the Hart-Scott-Rodino Antitrust Improvements Act. Appellants' analogy could not be more inapposite. There is no meaningful similarity between delays necessarily imposed by external and neutral regulatory requirements and delays operating at the option and for the benefit of a hostile target management. The extent of any delays created by the need to secure anti-trust approvals will not depend on whether a proposed acquisition is friendly or not. Conversely, the maximum delays permissible under the Indiana statute will occur only when target management wants them to and will serve no separate regulatory function.

6 Securities and Exchange Commission ("S.E.C.") regulations promulgated pursuant to the Williams Act provide that the bidder is not required to keep his tender offer open for more than twenty business days. See 17 C.F.R. § 240.14e-1(a) (1986).

Appellants further argue that, unlike the statute deemed unconstitutional in *MITE*, the Indiana statute does not delay commencement or even consummation of the tender offer. Under the statute, they claim, a bidder is free to close his offer within the Williams Act time frame and only his subsequent voting rights are affected. To the objection that no rational tender offeror will purchase shares when he doesn't know if he will ever be able to vote them, appellants offer a "practical alternative" (Brief of Intervenor-Appellant State of Indiana ("Indiana Brief") at pp. 62-73). They claim a purchaser can close an offer within the Williams Act's time frame but make his purchases of target's stock conditional on subsequent shareholder approval of his voting rights.

However, appellants' "practical alternative"—in itself, complex, burdensome, and unprecedented—ignores the basic negative qualities of delay in tender offer situations which have caused it to be termed "the most potent weapon" against hostile takeovers. Delay permits target management time to set up a wide array of defensive measures—ranging from corporate restructuring, to poison pills, to self-tenders, to defensive acquisitions—designed to irrevocably block and impede the takeover even if the shares already have been tendered. *See MITE*, 457 U.S. at 638 n.13. Such defensive actions can be as easily undertaken during the fifty-day delay prior to a shareholder vote under the Indiana statute as during a delay prior to the commencement or closing of a tender offer. The "practical alternative" offered by appellants therefore does nothing to cure the negative effects of the delays which this Court condemned in *MITE* but which the Indiana statute still permits target management to effect.

Furthermore, by excessively extending the period between the announcement of an intention to make a bid and the actual successful completion of the offer, the Indiana statute pro-

motes the very uncertainty and market volatility which the Williams Act was intended to minimize.[7]

C. The Second Generation Statutes Violate The Williams Act's Policy Of Investor Autonomy

The Indiana statute, moreover, conflicts with the Williams Act in an even more fundamental way. Thus, the Indiana statute clearly establishes as a practical matter that no tender offer can be consummated by any rational bidder absent a shareholder vote that will grant him the voting rights that are the reason for the offer in the first instance. This, in effect, requires the bidder to conduct and win a proxy contest with target management before he can purchase shares from any shareholders. Yet the Williams Act clearly intended that the decision to tender one's shares be one that rested with the *individual* shareholder alone and that it was *not* to be made subject, by statute, to another's control or veto.

Thus, one of the vices of the Illinois statute, as found by the plurality opinion in *MITE*, was that it made the individual shareholder's ability to accept a tender offer subject to the judgment of others—in that case, the Illinois Secretary of State:

> The Court of Appeals *understood the Williams Act and its legislative history to indicate that Congress intended for investors to be free to make their own decisions. We agree.* Both the House and Senate Reports observed that the Act was "designed to make the relevant facts known so that shareholders have a fair opportunity to make their decision." H.R. Rep. No. 1711, 90th Cong., 2d Sess., 4 (1968); Senate Report, at 3. Thus, as the Court of Appeals said, "[t]*he state thus offers investor protection at the expense of investor autonomy—an approach quite in conflict with that adopted by Congress.*"

Id. at 639-40 (emphasis supplied).

The individual shareholder's autonomy with respect to his investment decision is no less restricted by being made subject to the veto of other shareholders. This indeed has been the holding of the courts which, since *MITE*, have considered control share statutes similar to the Indiana statute. *E.g.*, *Fleet Aerospace Corp. v. Holderman*, 637 F. Supp. 742, 756 (S.D. Ohio), *aff'd*, 796 F.2d 135 (6th Cir. 1986) (Ohio Control Shares Acquisition Act unconstitutional on preemption grounds because "it prevents the individual investor from deciding whether to sell his or her stock . . . and places the decision in the hands of other shareholders of the target company."); *Icahn v. Blunt*, 612 F. Supp. 1400, 1420 (W.D. Mo. 1985) (Missouri statute unconstitutional where decision of "whether to buy or to sell [control shares] would be taken out of the hands of the shareholder and the purchaser and placed in the hands of management and other shareholders").

Appellants argue that whatever its purpose or impact, the Indiana statute is constitutionally acceptable because it purports technically to deal with the internal governance of corporate affairs, an area that is the exclusive domain of the states, rather than with the sale or acquisition of securities in a tender offer. Such an elevation of form over substance would, however, be an absurd constitutional principle: if it were accepted, a state could simply provide that a hostile offeror could never merge with the target company, never receive dividends, never have representation on its Board of Directors, or never be allowed to choose corporate officers, all matters which similarly can be said to be matters of "internal governance." The purpose and impact of a statute, and not its title or placement in the state statute book, obviously should determine its constitutional merits.

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7 Rule 14d-2, 17 C.F.R. § 240.14d-2 (1985), promulgated pursuant to the Williams Act, which requires a tender offer to commence not more than five days after public announcement of a bid, was adopted on the basis that longer delays would encourage excessive market and arbitrage activity and thereby "deny security holders the protections which that Act was intended by Congress to provide," Exchange Act Release No. 16384, 44 Fed. Reg. 70,326 (1979), at 70,329. In adopting Rule 14d-2, the S.E.C. stated an express intention to pre-empt state takeover statutes then existent which, by permitting longer delays, operated to "frustrate the operation and purposes of the Williams Act." *Id.* at 70,330.

Indeed, even if viewed mechanistically, the Indiana statute still would not pass constitutional muster, since it is directed not to corporate activity, but rather to the purchase and sale of shares among shareholders. Unlike staggered boards, cumulative voting, or supermajority provisions (corporate governance devices cited by appellants as within the state's power to legislate), which protect minority rights within a corporation by regulating the circumstances pursuant to which the *corporation* can undertake certain actions, the control share statutes operate to directly regulate and discourage transactions among individual shareholders.

Furthermore, unlike the control share statutes, the traditional corporate governance provisions cited by appellants do not operate primarily or exclusively against an acquiror seeking corporate control.[8] The Indiana statute however operates *solely* and *punitively* against a bidder for corporate control. Rather than incidentally affecting his ability to influence the operations of the corporation, it immediately and instantly—upon purchase of the control shares—eliminates the voting rights of his stock and his ability to exercise influence, let alone control, over the company. It is clear, in short, that "internal corporate affairs" is a mere facade for regulation designed directly to deter and delay hostile tender offers.

The State of Indiana does not, in fact, seriously dispute that this is the statute's purpose and effect. Thus, it concedes (Indiana Brief at pp. 91-95) that one effect of the Indiana legislation will be to substantially deter partial tender offers although such tender offers have been consistently recognized

8 Indeed, the effects of these common corporate governance provisions apply even where corporate ownership is diffused. A supermajority provision may operate just as well to prevent a merger favored by a majority of individual shareholders of a corporation as to prevent a merger favored by a single controlling shareholder. Indeed, such provisions can even benefit a potential acquiror. Thus, a potential acquiror holding 20% of a corporation's voting stock can benefit from an 80% supermajority merger requirement by being able to block a defensive merger undertaken by management. Similarly, cumulative voting guarantees him representation on the board even prior to his achieving a majority position. It is only the takeover statutes, such as the one at issue, which cut but one way—in favor of incumbent management.

as permissible under the Williams Act. And it admits further that the intent and "practical effect" of the statute is to replace the federal securities law policies of the Williams Act with the securities policies of the United Kingdom:

> [T]he Indiana Statute will have a practical effect analogous to that of legislation in the United Kingdom which requires majority shareholder approval of tender offers. The British regulations allow shareholders to simultaneously tender their shares and vote for or against the offer.

Indiana Brief at 95.

While economists might profitably argue the merits of the British approach versus the informed free-market policy embodied in federal law, it is respectfully submitted that the issue of the right of any state to make this choice was settled long ago in our federal Constitution. It is difficult to imagine a clearer violation of the Supremacy Clause than for a state, in a matter broadly affecting the national economy, to choose to adopt the legislative approach of a foreign power over that of the Congress of the United States.

In short, the clear legislative intent of the Williams Act and the reasoning underlying the plurality opinion in *MITE* mandate a finding that the Indiana statute upsets the balance struck by the Williams Act, and is, hence, unconstitutional.

II. THE INDIANA STATUTE VIOLATES THE COMMERCE CLAUSE OF THE CONSTITUTION

In *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 106 S. Ct. 2080 (1986), this Court, relying *inter alia* on its plurality opinion in *MITE*, recently reaffirmed the "two-tiered approach" traditionally followed in determining the constitutionality of state economic regulation under the Commerce Clause:

> When a state statute directly regulates or discriminates against interstate commerce, or when its effect is to favor

in-state economic interests over out-of-state interests, we have generally struck down the statute without further inquiry. When, however, a statute has only indirect effects on interstate commerce and regulates evenhandedly, we have examined whether the State's interest is legitimate and whether the burden on interstate commerce clearly exceeds the local benefits.

106 S. Ct. at 2084 (citations omitted). Under either of the two tests applied "the critical consideration is the overall effect of the statute on both local and interstate activity." *Id.*

In *MITE*, a majority of this Court determined that a state statute that regulated and restricted the purchase and sale of securities pursuant to a nationwide tender offer violated the Commerce Clause in that the substantial burdens it imposed upon interstate commerce outweighed the putative local benefits intended to be served by the legislation. This Court, by a plurality of four justices, additionally held that, irrespective of the balance of national and local interests, the state takeover statute violated the Commerce Clause, because such legislation constituted a direct, rather than incidental, regulation of interstate tender offers, a vehicle of interstate commerce.

As has been noted, the second generation post-*MITE* state takeover statutes, of which the Indiana statute is a fair example, differ only in form from the statute struck down in *MITE*; their intended and operative effects remain the same. The identical reasoning and constitutional considerations which impelled the overturning of the Illinois statute in *MITE* consequently mandate a similar determination with respect to the Indiana statute under review.

A. The Indiana Statute Is Unconstitutional Per Se As A Direct Burden on Interstate Commerce

[A] state statute which by its necessary operation directly interferes with or burdens [interstate] commerce is a prohibited regulation and invalid, regardless of the purpose with which it was enacted.

MITE, 457 U.S. at 642 (plurality opinion), citing and quoting this Court's decision in *Shafer v. Farmers Grain Co.*, 268 U.S. 189, 199 (1925).

The Indiana statute constitutes a direct burden upon interstate commerce in that the practical effect of the statute is to burden, regulate, and restrict interstate securities transactions outside the territorial jurisdiction of the state. That nationwide tender offers constitute interstate commerce was clearly determined by this Court's decision in *MITE* and cannot be disputed by appellants. 457 U.S. at 641-42 (plurality opinion).

Indeed, in the sheer multitude of its myriad securities transactions carried out across state lines and national boundaries, few business phenomena exhibit more of the characteristics of interstate and international commerce and less of the indicia of localized transactions than does the modern tender offer. The commerce in control shares generally does not involve discussions or negotiations in any particular locality. Buyers and sellers rarely if ever meet. The operative transfers of securities involved occur anonymously and often simultaneously on the floor of a national exchange or by mail or wire receipt of a transmittal form at the central offices of a designated depository.[9] The transactions of this nature involved in even a single moderate-sized tender offer may account for hundreds of millions of dollars in interstate commerce, and tender offers generate transactions involving many billions of dollars of interstate commerce yearly in the United States.

The drastic impact of control share statutes such as Indiana's on such interstate securities transactions simply cannot be questioned. The Indiana statute plainly restricts and burdens the ability of a bidder to purchase and the shareholder to sell, by means of a tender offer or other control share acquisition, securities of a target company. The Indiana legislation so

9 In nationwide tender offers, generally, the consummation of all sale and purchase transactions with respect to the shares tendered pursuant to the offer occur at a single moment, upon the expiration of the offer. At that moment, under the customary terms of the offer, the shares are deemed "accepted" for payment. Actual payment, usually by mail or wire transmittal, occurs shortly afterwards.

operates even though neither the bidder nor the majority of target's shareholders may reside in Indiana and although no operative act of the tender offer will occur in that state.

The Indiana statute accomplishes its burdensome and intrusive effect by granting to entities other than the bidder or the individual investor the ability to delay and thwart, as a practical matter, the tender offer or proposed stock transaction. Thus, as discussed above, under the statute, target management is given the power to delay consummation of the tender offer sufficiently beyond the periods mandated by federal law so as to facilitate defensive mechanisms that may permanently defeat the bid. The shareholder approval provisions further deter tender offers by denuding shares purchased pursuant to such offers of any voting rights, making the regaining of such rights subject to a subsequent vote by a majority of the other shareholders. At best, such provisions force the bidder to follow up his offer with an expensive and time-consuming proxy contest.[10] At worst, it may leave him, having already paid premium value, with "control" shares which give him no influence, let alone control, over the corporation.

The plain effect of these provisions, in most cases, will be that tender offers for target corporations subject to such statutes will simply not be made unless favored and approved in advance by incumbent management. In the rare event that an unsolicited tender offer is conducted, it will be made subject to the condition of subsequent shareholder approval, a condition that management, using the time provided by the statute's built-in delay, will seek to assure will never be met. The attendant difficulties and uncertainties created for the bidder will, in any case, virtually guarantee that, even where tender offers do proceed under the Indiana statute, a much lesser cash premium will be extended to shareholders in the offering price.

Although the Indiana statute's restrictive effect on nationwide tender offers is especially apparent, the statute's

10 Indeed, under the Indiana statute not only must the bidder bear his own expenses in such a contest but he must also give "an undertaking to pay the *corporation's* expenses" in calling and holding the required stockholders meeting. Ind. Code § 23-1-42-7(a) (1986) (emphasis supplied).

burdensome effect on interstate commerce is not restricted to its effect on tender offers alone. The Indiana statute would substantially deter any unsolicited acquiror from purchasing—on the open market, by privately negotiated transaction, or otherwise—any shares that would bring his total shareholdings in the corporation to over 20%. Yet the vast majority of transactions thus affected would clearly not involve Indiana residents or acts taking place in Indiana. The Williams Act, by contrast, only requires that full disclosure as to intentions and background of a holder of over 5% of an issuer's shares be made prior to any additional purchases. The substantial burdens added on by the Indiana statute clearly restrict, in a major fashion, the freedom of non-resident shareholders to engage in interstate commerce.

As the plurality in this Court determined in *MITE*, the imposition by a state of such extraterritorial burdens on a nationwide tender offer directly regulates and restricts interstate commerce and constitutes a *per se* violation of the Commerce Clause.

> [T]he Illinois law, unless complied with, sought to prevent MITE from making its offer and concluding interstate transactions not only with Chicago Rivet's stockholders living in Illinois, but also with those living in other States and having no connection with Illinois. . . . It is therefore apparent that the Illinois statute is a direct restraint on interstate commerce and that it has a sweeping extraterritorial effect.

MITE, 457 U.S. at 642.

The conclusions reached in MITE, it is submitted, apply equally to the 'second generation' statutes enacted to avoid MITE's clear impact. Such, at least, has been the consensus of the courts which since *MITE* have considered control share acquisition laws such as the Indiana statute. *See Fleet Aerospace Corp. v. Holderman*, 637 F. Supp. at 760-61; *Icahn v. Blunt*, 612 F. Supp. at 1415-16; *Dynamics Corporation of America v. CTS Corp.*, 794 F.2d at 264; *Terry v. Yamashita*, 643 F. Supp. at 165.

Appellants' contention that the Indiana statute does not regulate interstate commerce because it achieves its deterrent effect through elimination of voting rights rather than through a technical prohibition on the purchase or sale of the target's securities argues on behalf of a formalism which has long since been rejected by this Court. As this Court has made clear, it is not form but *practical effect* that will be determinative on the issue of whether a state's economic regulation impermissibly intrudes on interstate commerce. *E.g.*, *Southern Pacific Co. v. Arizona*, 325 U.S. 761, 775 (1945) (state law overturned on Commerce Clause grounds where "practical effect of such regulation is to control [conduct] . . . beyond the boundaries of the state . . . ."); *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 106 S. Ct. 2080 at 2086 (fact that New York law "is addressed only to sales of liquor in New York is irrelevant if the 'practical effect' of the law is to control liquor prices in other States."); *MITE*, 457 U.S. at 643 (plurality opinion).

In short, the Seventh Circuit's observation on the effect and operation of the Indiana statute is fully accurate:

> [I]n this case the effect on the interstate market in securities and corporate control is direct, intended, and substantial; it is not merely the incidental effect of a general regulation of internal corporate governance. The law in question is an explicit regulation of tender offers; that the mode of regulation involves jiggering with voting rights cannot take it outside the scope of judicial review under the commerce clause. Any other conclusion would invite facile evasions of the clause.

794 F.2d at 264. The Indiana statute, as a direct state attempt to regulate interstate commerce, is thus unconstitutional *per se*.[11]

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[11] Appellants' recurrent emphasis that the Indiana statute must be constitutional because it is 'non-discriminatory' is merely a red herring. The Indiana statute is offensive to the Commerce Clause not because it discriminates against other states but because it operates to burden and regulate interstate commerce, which alone is sufficient to violate the Commerce Clause. Lack of discrimination only becomes an

B. No Significant Local Benefits Exist Which Outweigh The Indiana Statute's Substantial Interference With Interstate Commerce

In *MITE* this Court determined that no local benefits purportedly conferred by "first generation" takeover statutes, such as the Illinois law overturned in that case, were commensurate with the statutes' "substantial" adverse effects on interstate commerce. These adverse effects were, in the Court's view, drastic in impact and national in scope, affecting both target shareholders and the national economy as a whole:

> The effects of allowing the [state regulatory authority] to block a nationwide tender offer are substantial. Shareholders are deprived of the opportunity to sell their shares at a premium. The reallocation of economic resources to their highest valued use, a process which can improve efficiency and competition, is hindered. The incentive the tender offer mechanism provides incumbent management to perform well so that stock prices remain high is reduced.

457 U.S. at 643.

Such negative impact on non-resident shareholders, non-resident bidders and the United States economy were, this Court observed, offset by no substantial countervailing local benefits conferred on the state or its residents: "Insofar as the Illinois law burdens out-of-state transactions, *there is nothing to be weighed in the balance to sustain the law*." *Id.* at 644 (emphasis supplied).

The burdensome impact on interstate commerce created by control share statutes such as Indiana's is identical to, if not greater than, those arising out of the "first generation" pre-*MITE* statutes. Indeed, appellants do not seriously contend that the national market in control shares will continue undis-

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issue where, as in *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117 (1978), the statute is designed to affect transactions occurring solely within a state's own borders and thus, absent a discriminatory effect, would pose no constitutional problem.

turbed in the face of these "second generation" statutes. Nor, indeed, do they set against this substantial interference with interstate commerce any substantive local benefits allegedly accruing from the Indiana legislation. Appellants rather respond with a talismanic formula—the "internal affairs" doctrine—the mere invocation of which they suppose sufficient to dissipate all constitutional concerns like so much mist.[12]

12 Indiana, while not seriously claiming that its legislation will leave tender offers unaffected, puts forward the unique suggestion that the Indiana statute will facilitate rather than impede corporate takeover acquisitions. Making the Indiana statute sound like nothing so much as a Hostile Bidders' Bill of Rights, the State stresses that the law allows offerors an "immediate shareholder vote on the merits of their offers," and that the moral suasion flowing from a favorable vote in this plebiscite will make it more difficult for management to "wage war" against a hostile bid. (Indiana Brief at pp. 75-76). Indeed, Indiana suggests that, by mandating a shareholder vote on voting rights, within "only" 50 days, the "months-long" duration of "bitterly fought takeover battles" will be truncated (Indiana Brief at p. 102).

This prognosis is not only disingenuous in concept, but also flies in the face of logic and experience. Under the federal regulatory scheme tender offers are not required to remain open longer than twenty business days, approximately half the time span provided for by Indiana's provision for an "immediate" shareholder vote. If some tender offers now extend beyond the Williams Act's twenty day period it is primarily because (a) other bidders have arisen and a prolonged auctioning process has ensued; (b) legal deficiencies, such as securities or anti-trust violations, have been found to exist in the bidder's offer; or, most commonly, (c) target management has put in place defensive strategies, in the form of poison pills, self-tenders, or the like, and consummation of the tender offer is made to await judicial determinations as to the propriety of these entrenchment measures designed "to wage war" against the offer. Statutes such as Indiana's obviously do nothing to eliminate the first two of these causes of delay and would *contribute* to the final cause by giving target management more time to implement defensive tactics, generating even further delay.

In sum, the argument that the statute is intended to confer benefits on hostile acquirors is as much of a facade as the statute itself. Far better the candor of the Indiana Chamber of Commerce, which participated in the formulation and drafting of the statute, and which concedes in its *amicus* brief (at p. 18 n.9) that one of the purposes of the statute was "protecting the quality of corporate governance in Indiana *by granting certain protections to corporate directors*" (emphasis supplied).

Thus, appellants contend that because the Indiana statute on its face deals with voting rights of shareholders, which appellants claim, under the "internal affairs" doctrine, to be the province of the states, the practical effect of the statute to deter and burden extraterritorial interstate securities transactions may be conveniently ignored. Appellants' argument proves too little, too much, and, ultimately, nothing at all.

As this Court observed in *MITE*, when faced with the identical argument, the internal affairs doctrine is not a concept relevant to constitutional law but a principle of the conflict of laws. Such principle apportions the power to regulate corporations *between* the States so as to avoid inconsistent rulings or legislation:

> The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation's internal affairs—matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders—because otherwise a corporation could be faced with conflicting demands. *See Restatement (Second) of Conflicts of Laws* § 302, Comment b, pp. 307-308 (1971). That doctrine is of little use to the State in this context. Tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company.

457 U.S. at 645.

There is no basis for attaching to this doctrine constitutional implications. That courts will apply Delaware law to Delaware corporations and Indiana law to Indiana corporations does not mean that either Delaware or Indiana is permitted to enact, under an "internal affairs" rubric, corporate laws that, in violation of the national Constitution, impermissibly intrude upon interstate commerce. The danger of inconsistent rulings which the internal affairs doctrine was intended to minimize is simply not implicated where an area is determined by the Commerce Clause to be the province of federal jurisdiction to the exclusion of that of *any* of the states.

Thus, even were the instant statute predicated on a good faith concern with respect to the internal affairs of Indiana corporations, this would, nevertheless, still not provide the Indiana legislature with *carte blanche* to ignore constitutional limitations and intrude upon interstate commerce.[13] In the instant case, however, appellants' attempts to justify the Indiana statute under the pretext of the internal affairs doctrine are in any event a mere charade. Even the enacters and enforcers of second generation statutes such as Indiana's do not pretend that their statutes are not designed to regulate and restrict hostile tender offers. As noted above, Indiana itself admits that the practical effect of its legislation is to substantially deter otherwise legitimate partial tender offers and to implement a British approach to tender offers by requiring majority approval of shareholders for the sale of control shares.

Similarly, the State of Minnesota, which has enacted a second generation control share statute of its own, admits in its *amicus* brief to this Court ("Minn. Brief") that the purpose and effect of such statutes is to "inhibit the abusive use of takeover tactics" and to mitigate the supposedly "coercive nature of control share acquisitions" (Minn. Brief at 11). The State of New York, as noted, has similarly admitted, for its own part, that the effect of its legislation is to "discourage unilateral takeovers" (*supra* at p. 8 n. 3). It is thus clear that the states themselves do not deny the fully-intended impact of their control share statutes on tender offers.

That the State of Indiana effects such regulation of tender offers through *in terrorem* provisions respecting essential voting rights rather than by directly prohibiting purchases of the tendered shares themselves makes, as has been noted, no

13 *See*, for example, *Brown-Forman Distillers*, where, despite the "wide latitude" given the States under the Twenty-First Amendment "to regulate the importation and distribution of liquor within their territories," this Court overturned provisions of a New York law regulating the sale of liquor on the basis of the statute's "practical effect" on interstate commerce. 106 S. Ct. at 2086.

practical or legal difference. It is as if a state rather than prohibiting the rental of automobiles permitted their rental—but with their engines removed. As the State of Minnesota has stated in the *amicus* brief it has filed *on behalf of* Indiana's position (*id.* at 15), to attempt any distinction of the Indiana statute on this basis "elevates form over substance":

> Although the [Indiana statute] does not actually require shareholder approval prior to the control share acquisition, the practical effect of the Indiana statute may be just that.

Id. at 15 n.15.

If the practical effect of a state statute is to regulate and restrict tender offers, the nature of the particular device effecting such regulation, or the chapter heading of the corporate statute pursuant to which it takes place, cannot be of any constitutional significance. To accept otherwise is to open the door to wholesale regulation of interstate commerce by any state willing to cloak its economic regulation under an appropriate facade. A state, under such a theory, would presumably have the constitutional authority to permanently strip control shareholders of voting rights upon a vote, not of the majority of shareholders, but simply of the incumbent board of directors. For that matter the rights could be removed without recourse to any vote at all, if the state determined that this were an appropriate policy. Nor would a state's regulation be limited to removal of voting rights; it could choose to strip the bidder of dividend rights or of any of the other indicia of ownership as well.

Appellants' invocation of such traditional state corporate governance rules as supermajorities and cumulative voting, as examples of permissible internal governance statutes which impact on interstate commerce, does nothing to support their contentions. As has been noted, such true corporate governance statutes, which genuinely seek to regulate the internal operations of the corporation, bear no relation to the Indiana statute's direct attempt to influence the purchase and sale of

securities between *shareholders* of the corporation and other shareholders or third parties. Indeed, these statutes demonstrate the power of the states to adequately legislate internal corporate governance to protect minority shareholders without recourse to legislation designed to obstruct the interstate securities market or national tender offers.[14]

Similarly, it adds nothing to appellants' arguments to point out that the voting rights stripped away by the Indiana statute in control share transactions are themselves creatures of state corporate law. Such an argument proves too much, since the same could be said with respect to any of the rights attached to corporate securities. Indeed, such securities themselves, as an ultimate matter, are nothing more or less than an agglomeration of various contract and property rights, all created and sustained under state law. This meta-legal truth, however, has never caused this Court or Congress any hesitation in considering transactions involving the sale or purchase of these bundles of rights as interstate commerce. Indeed, the extensive federal regulation of the securities markets, including the Williams Act, is based squarely on the assumption that such transactions do constitute interstate commerce.

In sum, the balancing test required under the Commerce Clause for the Indiana statute is no different than that which was undertaken by this Court in *MITE*. As in *MITE*, the statute here is clearly unconstitutional.

14 The attempt to support the Indiana statute as an exercise in "shareholder democracy" (*see, e.g.*, Minn. Brief at p. 11) is particularly disingenuous, especially in view of the act's direct effect and intent to disenfranchise shareholders who would otherwise possess over 20% of the shareholder vote, a singularly undemocratic provision.

CONCLUSION

This Court should affirm the judgment below.

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